INVESTOR PROTECTION IN THE NAFTA AND BEYOND:

Private Interest and Public Purpose

Alan S. Alexandroff, Editor

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Foreword

One of the important — and controversial — legal rights provided by the North American Free Trade Agreement (NAFTA) was accorded to investors residing in one NAFTA country and investing in another. The trade pact provides opportunities for foreign investors from a NAFTA country to sue governments for compensation when a host country discriminates against them. Since NAFTA was concluded, this right has been both praised and condemned. Does this provision limit government's ability to regulate in the public interest? Or does it enhance sovereignty by ensuring that governments follow rules laid out by the treaty?

The contributions in this book suggest that the tribunals have made judgments that are largely fair to both investors and governments. Canadian investors in Mexico and the U.S. have been able to protect their investments, while foreign investors in Canada have done likewise.

Protection of investor rights will continue to be an important issue in current and future trade negotiations throughout the world. The ability of foreign investors to seek compensation if their rights are violated enables businesses to operate in jurisdictions with some confidence. Not only is this a topic discussed at the World Trade Organization but it has also been discussed in many bilateral negotiations. Canada's experience in NAFTA may be a useful guide to Canada and other countries as they develop treaties in the future.

This book, which is based on a conference held by the C.D. Howe Institute and the Munk Centre for International Studies at the University of Toronto, provides a good review of the various cases and issues that have arisen from the investor protection provisions of NAFTA. I wish to thank Alan Alexandroff, our Fellow-in-Residence on international policy, who organized both the conference and the book. I also wish to thank the participants who have provided thoughtful discussion of this provision and its implications for Canada's public policies. Thanks to Kevin Doyle, Sheila Protti, James Fleming, Wendy Longsworth and Diane King for editing and preparing the manuscript for publication.

The C.D. Howe Institute gratefully acknowledges the Donner Canadian Foundation for its support of the Institute's *Border Papers* and in particular the conference on investor protection at the Munk Centre for International Studies that was the original impetus for this book.

As usual, the views expressed in this book are those of the editor and authors and should not be attributed to the C.D. Howe Institute or its Board of Directors.

Jack M. Mintz
President and
Chief Executive Officer

Acknowledgments

This book, or at least the idea for it, began some time ago. Yet completion turned out to be much longer than I anticipated in the spring of 2001 when I formally initiated *Investor Protection in the NAFTA and Beyond: Private Interest and Public Purpose.* Since then, the pace of investor claims in North America has slowed noticeably, as have the decisions arising from the tribunals established to hear the complaints. Thus, the examinations by our authors of the tribunal judgments remain focused on the critical tribunal decisions. Most importantly, the political and civil society contention surrounding investor protection remains, even though the public debate has muted. The examination in this volume, in fact, strips away what now appears to have been excessive rhetoric to reveal some of the positive aspects of investor protection and questioning, in particular some of the tactics and strategy of the Canadian government.

On a personal level, the idea to examine investor protection grew out of both private experience and public activity. For a number of years I acted as outside Counsel to Appleton & Associates. Barry Appleton, the managing partner of the firm, early on saw the possible protections for foreign investors in North America under the investor-state provisions in Chapter 11 of the North American Free Trade Agreement (NAFTA). In fact, as early as 1996, Ethyl Corp. engaged his law firm to examine its rights under these investment protection provisions. A Notice of Intent to Submit a Claim was served on the Government of Canada on September 10, 1997 and a Statement of Claim was served on October 2, 1997.

With this action underway, something of a phenomenon in Canadian public policy and politics was born. What had begun as a little heralded section of NAFTA quickly gained notoriety — much of it negative. Indeed the investor complaints and tribunals that followed, despite being confidential (an issue itself of concern raised by civil society groups), gained Chapter 11 much public attention in all three North American polities. A rising chorus of comment, indeed alarm, issued from a variety of civil society interests especially but not only from the environmental community.

The governments, or NAFTA parties as they are formally known, began to discuss between themselves and in public the cases and rights afforded by the Chapter 11 provisions. This rising clamor from the public, the government, as well as legal and public policy analysts also caught my attention. In what I had perceived to be a rather arcane area, investor protection rights seemed transformed almost overnight into the 'infamous Chapter 11 cases'.

In the summer of 2000 I approached Jack Mintz — a friend and colleague and the CEO of the C.D. Howe Institute — to suggest that the Institute examine the question of investor protection. He, along with senior staff at the C.D. Howe but especially Senior Vice President Bill Robson, was then just organizing what became the Border Papers. This series examines Canadian policies in the North American economic context. Jack and Bill suggested that we organize a conference on investors, investments and investment protection in NAFTA. That proposal initiated the activity that has now finally led to this book.

To plan a conference where a variety of views over investor protection could be aired, I turned to Professor Lou Pauly, Chair of the Centre for International Studies at the Munk Centre for International Studies at the University of Toronto. With his assistance we organized a conference which included then-minister of international trade, Pierre Pettigrew. It is always somewhat daunting to include public officials, given their demanding schedules, so we decided to hold a preliminary meeting for Minister Pettigrew alone and then organize a subsequent full conference.

On September 28, 2001, Minister Pettigrew, just a little over two weeks after the terrible shock of September 11, addressed a public audience to deliver the speech on investor protection found in this volume. With the minister's speech, planning for the full conference was well underway. On May 3, 2002, participants gathered at the Vivian and David Campbell Conference Centre at the Munk Centre for International Studies to discuss investor protection. The conference was sponsored jointly by the C.D. Howe Institute and the Centre for International Studies at the Munk Centre for International Studies at the University of Toronto. The early part of the conference focused on what I call in this volume the *micro* aspects of investment protection, including the substantive and procedural aspects of NAFTA Chapter 11 itself as well as the arbitral and legal decisions and interpretations of the Chapter 11 cases. Related to those micro aspects, participants also discussed Canadian policies towards investor protection and the influence of investor protection cases on those policies. Finally, towards the end of the day participants explored investment protection beyond North America — what I call the *macro* aspects of investor protection. Indeed, this final session examined the question of investment and investment protection in the multilateral setting, particularly the WTO.

It was this last arena — the multilateral negotiations over investment — that was responsible, in part, for the delay in bringing the book to completion. By the fall of 2003 we appeared to have reached a moment of closure on multilateral investment: The breakdown in negotiations at Cancun. The tortured path of multilateral negotiation did, however, give us the chance to reshape a few contributions. We added some comments, even though they had not been presented at the conference, in order to fill out some of the subjects we had explored initially at the conference.

Despite the lengthy gestation period for the book, its appearance is opportune. After the first series of disputes against Canada were launched, a significant number of studies have been published.[1] The Government of Canada supported a number of inquiries and public discussions. For example, the Department of Foreign Affairs and International Trade (DFAIT), as it was previously called, supported a conference on NAFTA's Chapter 11 at the

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[1] The number of legal articles has increased over the years since NAFTA came into force. The volume is far too numerous to catalogue here. I shall note only a few recent examples here. Reference should be made to legal periodicals to examine the full extent of legal analysis: Marcia J. Staff & Christine W. Lewis, "Arbitrations Under NAFTA Chapter 11: Past, Present, and Future," *Houston Journal of International* Law, Vol. 25 (2003), Chris Tollefson, "Metalclad v. United Mexican States Revisited: Judicial Oversight of NAFTA's Chapter Eleven Investor-States Claim Process," *Minnesota Journal of Global Trade*, Vol. 11 (2002), David Gantz, "Reconciling Environmental Protection and Investor Rights under Chapter 11 of NAFTA," *Environmental Law Reporter*, Vol. 31 (2001), ...

Centre for Trade Policy and Law in January 2002, which resulted in a full volume on Chapter 11 cases. On a formal level, the Government began to explore possible changes or clarifications to Chapter 11. After several meetings of the NAFTA Free Trade Commission (FTC), the Commission published *Notes of Interpretation of Certain Chapter 11 Provisions* in July 2001. This action undertaken by the trade ministers of the NAFTA parties, pursuant to Chapter 11, sought to clarify a number of provisions including the meaning of the minimum standard of treatment and the provisions for transparency under Chapter 11. This has not, however, ended the FTC's or the NAFTA parties' review of the operations and implementation of the investment chapter. The parties established the NAFTA Investment Experts Group (IEG), composed of government officials from the three NAFTA parties, to conduct a review. Among other things, the IEG decided to seek civil society views, and so, Canada hosted a trilateral multi-stakeholder consultation in Montreal in May 2003. This broad expert and civil society con-

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footnote 1 cont'd

... Todd Weiler, "NAFTA Article 1105 and the NAFTA Free Trade Commission: Just Sour Grapes, Or Something More Serious?" *International Business* Lawyer, Vol. 29 (December, 2001), Todd Weiler, "Metalclad and the Government of Mexico: A Play in Three Parts," *Journal of World Investment*, Vol. 2 (2001) and Todd Weiler, "The Ethyl Arbitration: First of Its Kind and a Harbinger of Things to Come," *American Review of International Arbitration*, Vol. 34 (2001). From a business and management perspective Professor Alan Rugman has been an acute observer of the impact of investment protection on business strategies: see his edited volume Foreign Investment and NAFTA, (South Carolina Press, May 1994). More recently a series of volumes have appeared that attempt to evaluate the consequences of investor protection pursuant to Chapter 11 NAFTA. These volumes include: International Institute for Sustainable Development, *Private Rights, Public Problems: A Guide to NAFTA's Controversial Chapter on Investor Rights*, (Winnipeg, Manitoba: International Institute for Sustainable Development and the World Wildlife Foundation, 2001), Laura Ritchie Dawson with an introduction by Donald M. McRae, ed., *Whose Rights?: The NAFTA Chapter 11 Debate*, (Ottawa: Centre for Trade Policy and Law, 2002) (*Whose Rights*), Julie Soloway, Chris Tollefson, "NAFTA's Chapter 11: Investor Protection, Integration and the Public Interest," Choices: IRPP, Vol. 9, No. 2 (March, 2003) and Todd Weiler, ed., *NAFTA Investment Law and Arbitration: Past Issues, Current Practice, Future Prospects* (New York: Transactions Publishers, 2004).

sultation addressed both procedural and substantive issues. In addition, the three governments carried out various domestic consultations. The Canadian government organized an expert group, the Ad Hoc Expert Group on Investment, to assist the government in considering recommendations for changes to Chapter 11 and other investment agreements.

For now, we appear to be in a hiatus or quiescent period concerning NAFTA Chapter 11 and investment protection generally. An assessment of where investment protection is going in the multilateral context is necessary for an understanding of the path and consequences of investment protection in the North American economic space. At least for the immediate future, and given the results and follow-on from the Cancun Ministerial, there will not be a multilateral agreement on investment in the WTO. In addition, Canada's minister of international trade, responsible for trade and investment policy from 1999 through the end of 2003, departed office with the defeat of the Liberal government in 2006. Pierre Pettigrew was a vocal international trade minister. He spoke widely on Canada's trade and investment policies (and, as mentioned, participated in the activities that led to this publication).[2] Now is a good time to assess trade policy during his tenure and to look forward to its likely development in the years ahead.

Finally, some of the broader public debate has quieted down. What is left, however, is a trail of, in some instances, quite voluble criticism and evident concern about investment protection generally and about Chapter 11 specifically. In addition, there has already been a significant public examination. The Standing Committee on Foreign Affairs and International Trade undertook a parliamentary inquiry of North American trade, holding extensive hearings that enabled many civil society groups to speak out. That inquiry specifically examined NAFTA Chapter 11, among other areas. The Committee's report was released in December 2002 and made a specific recommendation for Chapter 11. The government responded to this recommendation in June 2003. Given these airing of views, we can assess the Chapter 11 cases and the consequences of Chapter 11, as conference participants and other authors do in this volume.

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[2] In addition, Minister Pettigrew examined the current context of Canadian politics in a book. See *The New Politics of Confidence* (Toronto: Stoddart, 1999).

A book like this cannot appear without the effort of many people. Obviously my first thank-you goes to all the speakers at the Munk Conference Centre and all the authors in this volume. I appreciate their patience greatly. I especially would like to thank Minister Pettigrew. Though we have been friends over many years, he had a hectic schedule and I appreciate his willingness to make himself available. I would also like to thank members of his staff, Jim Anderson and Andre Albinati, for ensuring that the minister made it to the Munk Centre with remarks in hand. I also want to express my gratitude to many at the Munk Centre. I would like to thank in particular the Director of the Munk Centre for International Studies, Dr. Janice Stein, for making the Conference facilities available. I appreciate the cooperation and co-sponsorship of Dr. Lou Pauly, the Director of the Centre for International Studies (CIS). Lou not only worked through ideas on investment protection, but also contributed directly to this volume. On the administrative side, I would like to thank in particular Tina Lagopolous of CIS and Mary Lynne Bratti of the Munk Centre for International Studies.

From the C.D. Howe Institute, I appreciate especially the patience and support of Jack Mintz, the Institute's President and CEO, and Bill Robson, Senior Vice President and Director of Research. Without their support this project would not have finally come to fruition. I would also like to express my appreciation to Institute Senior Policy Analyst Danielle Goldfarb for her willingness to consider new ideas for the volume on any given day. Finally, I would like to express my thanks to Kevin Doyle and Sheila Protti for their excellent editorial work, and to Wendy Longsworth and Diane King for preparing the manuscript for publication. Their work has improved immeasurably the quality of the volume.

I am unable to utter the usual disclaimer that the views expressed here are mine alone and that I am responsible for any errors or omissions. It is, of course, not possible in such an edited book. I do express my responsibility for the introduction and conclusion. Any errors or omissions in both are mine and mine alone and not the responsibility in any way of the authors of other chapters.

Alan S. Alexandroff
Editor

Introduction

Alan S. Alexandroff

If the authors in this volume had written or talked about the North American Free Trade Agreement's (NAFTA) Chapter 11 less than 10 years ago, the legal expert for sure, but just as likely the man in the street, would have assumed that the focus of this book concerned questions of insolvency and bankruptcy under United States law. Today in Canada, however, that is certainly not the case. For experts and the public alike, Chapter 11 references invoke almost instant response about the now rather infamous chapter in NAFTA on investment.

The essays in this volume concern investor protection. Investor protection and the national and international regulations that cover such protection are related to, though distinct from, investment and investment agreements. There are numerous statutes that examine and regulate investment. In Canada's past, for instance, there are a number of such statutes such as the *Foreign Investment Review Act* (FIRA) (c. 46 as amended), which became the *Investment Canada Act* (ICA) (c. 20 as amended).[1] These laws regulate investment in Canada. FIRA was particularly noteworthy in its screening of foreign investment and efforts to extract benefits for Canadians in agreements with foreign investors. Indeed, these benefits are what current investment protection statutes refer to as performance requirements. Unlike the earlier statutes, investment protection regimes target performance requirements and endeavour to restrict governmental action.

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[1] Stephen Brereton, the then-Director of the Investment Trade Policy Division of the Department of Foreign Affairs and International Trade (DFAIT), in his chapter in this volume, notes that the current threshold of review for WTO countries is at about $218 million in company assets.

The essays here are concerned with the protection of investors and their investments in the three NAFTA members — the United States, Canada, and Mexico. The rights and obligations have been articulated in international law principally through bilateral investment treaties.[2] Notwithstanding some recent legal argument these obligations are not particularly controversial.[3] They include non-discrimination provisions such as national treatment and most favoured nation treatment, minimum standard of treatment (MST) provisions, prohibition against certain performance requirements, expropriation and compensation provisions, and finally and significantly some form of investor dispute settlement provisions extending a right to investors to seek compensation where the investor believes that its investment has been harmed substantially. Though these substantive rights and obligations are non-controversial, the protections afforded foreign investors through NAFTA's Chapter 11 are controversial. Chapter 11 is embedded in a major trade agreement and has engendered controversy in no small measure because it imposes on each NAFTA member — technically referred to as a party — positive obligations and proscribes certain government behaviour while at the same time affording private parties the opportunity to seek compensation through arbitration. As the authors of this volume describe, there are a variety of concerns raised by the governments and national civil society interests over these investor-state provisions. But generally the wide opposition to these provisions arises because there are private protections, often more pointedly identified as corporate rights, that in some manner do or might limit public — that is, governmental — behaviour, objectives, and purposes.

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[2] A number of the papers in this volume note the enormous increase in the number of what Americans call bilateral investment treaties (BITs). These same agreements in Canada are called foreign investment promotion and protection agreements (FIPAs). As Brereton indicates at the beginning of his chapter, though there were fewer than 400 BITs at the beginning of the 1990s, by 2003 the total had surpassed some 2,200 bilateral agreements. As of 2005, Canada had 22 FIPAs in force.

[3] The controversy was addressed in the interpretation by the three member countries as the Free Trade Commission in the July 31, 2001 *Notes of Interpretation of Certain Chapter 11 Provisions*, (Interpretive Note). Its interpretation, in part, concerns the scope of rights and obligations related to the Minimum Standard of Treatment (NAFTA 2001).

As we will see, the controversy of private rights in the context of public purpose and objectives has not only been raised in the NAFTA context, but more recently has been extended in regional trade and investment negotiations such as the Free Trade Area of the Americas (FTAA), Asia Pacific Economic Cooperation (APEC), the Association of Southeast Asian Nations (ASEAN), and the Southern Cone Common Market (MERCOSUR). The controversy has also reached the multilateral settings, including the defunct Multilateral Agreement on Investment (MAI) in the Organisation for Economic Co-operation and Development (OECD), and in the World Trade Organization (WTO) in the discussion of investment in the Doha Development Round of negotiations.

While investor rights protected in NAFTA are not in any way unique, placing these rights in the context of a major trade agreement is, or at least was. In addition, in applying these investor protections to foreign investors in developed settings — here in Canada, and the United States — Chapter 11 is set off from the multitude of bilateral investment agreements.[4] The failure of the MAI, the lack of an FTAA[5] or the threat to exclude the Singapore issues[6] including investment from the current multilateral trade negotiations at the WTO, means that NAFTA provides an almost singular opportunity to evaluate investor protection in a developed country context.

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[4] Possibly the oddest of these is the newly minted United States-Australia Free Trade Agreement, which came into force on January 1, 2005. While investors receive substantive investment protections, they are not accorded specific dispute settlement procedures — namely investor state arbitrations. On the U.S.-Australia Free Trade Agreement, the United States Trade Representative's (USTR) *Trade Facts* notes that due to the "long-standing economic ties," "shared legal traditions," and the "confidence of their investors in operating in each others' markets," the parties agree not to provide such an arbitration procedure (USTR 2004). In other words, investors are reliant on U.S. and Australian courts and state-to-state dispute settlement procedures at least for now. While the full story is still emerging, it appears that Australian negotiators were adamant that investors only have recourse to national courts or, in the alternative, substantive protections would be provided through a state-to-state dispute-resolution procedure.

[5] This failure to complete the FTAA was underscored in the November 2005 meeting of Western Hemispheric leaders in Mar del Plata, Argentina. The summit broke up without a clear agreement even on how to resume stalled talks.

[6] Arising from the 1996 Singapore Ministerial, the "Singapore Issues" are investment, competition, government procurement, and trade facilitation.

This book is divided into a number of distinct subject areas. The first involves the micro issues. Without any pejorative connotation intended, the first set of authors, Barry Appleton, managing partner of Appleton & Associates; Milos Barutciski of Davies Ward Phillips and Vineberg LLP; and Ian Laird, formerly of Appleton & Associates, and currently at Davis and Company, focus on the Chapter 11 complaints and disputes against the three NAFTA parties, but examine most closely the cases against the Canadian government. Ian Laird, in fact, tackles a major Canadian government assertion that Canada's trade and investment policy relies on and supports a rules-based global trade regime. In that regard Mr. Laird's arguments represent a bridge to Canadian government policy over investor protection. Professor Stephen Clarkson of the University of Toronto places his argument in a broader context. He examines the impact of Chapter 11, and indeed the entire NAFTA treaty, on Canadian government policy. He argues that Chapter 11 and other aspects of NAFTA constitute a taking of a different sort. Professor Clarkson argues forcefully "...that NAFTA so closely conforms to the conventional notions of what comprises a constitution that it can best be understood as creating an external constitution for its signatories."

A second area of examination analyzes the effort in and possible consequences for advancing investment protection through a multilateral context — what is referred to elsewhere as the macro issues. Investment and investment protection have not been contentious issues only in the North American context. It has been for some time a much fought over issue multilaterally. In this volume, John Hancock, Counsellor in the Trade and Finance Division of the WTO Secretariat, and Professor Lou Pauly, Director of the Centre for International Studies at the Munk Centre for International Studies, University of Toronto, examine the future of investment protection in the multilateral setting.

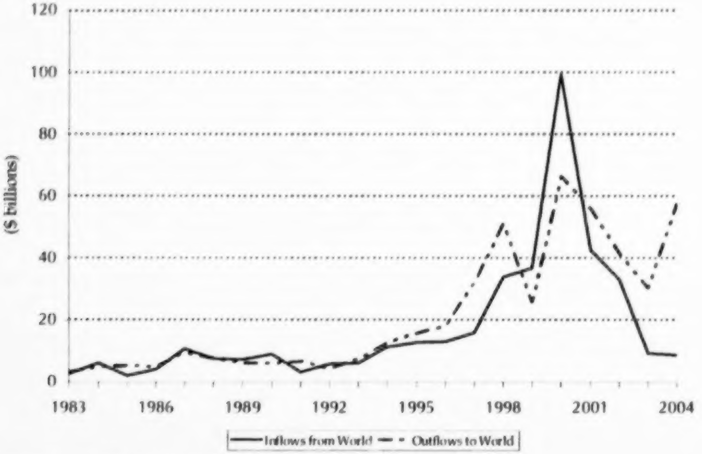
The final subject area focuses on Canadian government policy toward trade and investment generally, but particularly with respect to investment protection under Chapter 11. While this volume, and the 2002 Munk Centre Conference that convened earlier, did not specifically focus on Canada's trade and investment policy, the two analyses bookend the tenure of International Trade Minister Pierre Pettigrew, as noted in the Foreword. A number of the chapters focus on the declared Canadian trade and investment policy or on Ottawa's defence of actions and alleged behaviour raised by investor complainants, or shortcomings described by critics of the federal government and its trade and investment policy. This section includes the speech by then-Minister Pettigrew, delivered at the Munk Centre for International Studies, a chapter by Stephen Brereton, then-Director, Investment Trade Policy Division in the Department of Foreign Affairs and International Trade (DFAIT) (since possibly divided into the foreign affairs department and the international trade department), and a critical examination of the Canadian government's policies towards Chapter 11 by Professor Gilbert Winham, Eric Dennis Memorial Professor of Government and Political Science, Dalhousie University.

Trade and Investment Context

Figures 1 through 4 display Canada's foreign direct investment flows over the past two decades. These emphasize how the United States represents the dominant investment market for Canada. As Table 1a and 1b set out, the United States represents 43.6 percent of the stock of Canadian direct investment abroad, followed distantly by the UK, ranked as second, with a little under 10 percent of the stock of Canadian direct investment abroad. In terms of foreign direct investment in Canada the United States is even more dominant with more than 65 percent of the stock, followed distantly by the UK. The UK possesses about 8 percent of the stock of FDI in Canada.

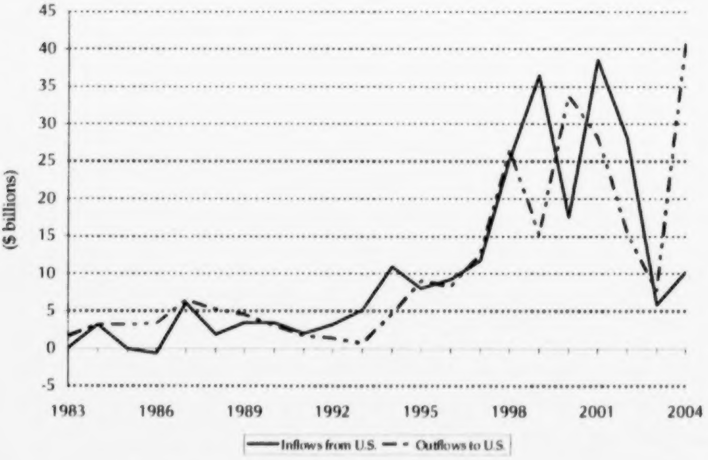
In summary, the trade and investment statistics underline that Canada is a highly open economy. As our politicians and trade negotiators constantly point out, we are one of the most open

Figure 1: *Foreign Direct Investment — Canada and the Rest of the World (1983 – 2004)*



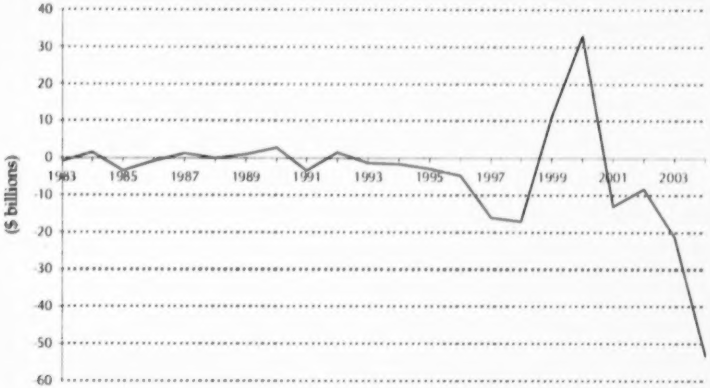
Source: Statistics Canada.

Figure 2: *Foreign Direct Investment — Canada and the United States (1983 – 2004)*



Source: Statistics Canada.

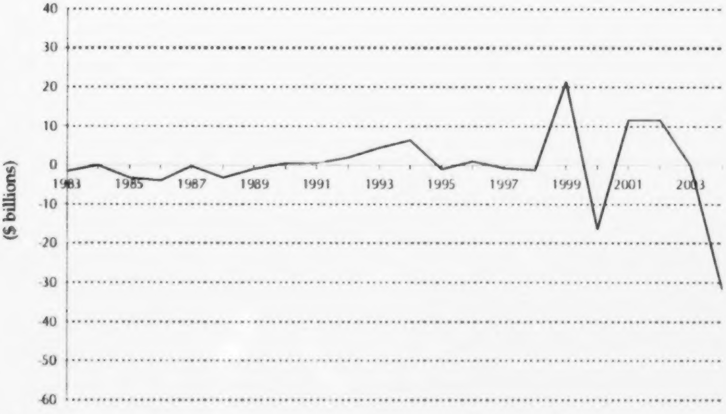
Figure 3: *FDI Balance* — Canada and the Rest of the World (1983 – 2004)*



Source: Statistics Canada.

Note: *A positive balance means that inflows from all countries are larger than outflows to all countries.

Figure 4: *FDI Balance* — Canada and the United States (1983 – 2004)*



Source: Statistics Canada.

*A positive balance means that inflows from the U.S. are larger than outflows to the U.S.

developed economies in the global trading system. Thus, Canada's trade-to-GDP ratio is approximately 80 percent; in the U.S., it is around 25 percent. As a result, these same politicians and trade officials often describe Canada as a global trader. However, the global statistics make clear that Canada trades primarily with one country — the United States. Trade statistics underline this highly integrated trade pattern. In 2004, almost 80 percent of Canada's total exports of goods and services went to the United States (in 1989 the figure was 71 percent).[7] Furthermore, all regions of the country have significantly increased trade with the United States, as have most industrial sectors. Analysts have noted the growing percentage of provincial trade directed to the United States for sev-

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[7] This statistic has to be understood in the context of the growing integration of the three NAFTA countries. There has been a significant integration of North American transportation, including the major railroads, since the signing of NAFTA. As a result, Canadian goods bound for the rest of the world are increasingly moving through U.S. ports. The trade statistics do not differentiate between goods from Canada that have the U.S. as a final destination and goods destined for the rest of the world. The Fourth Annual Report on Canada's State of Trade states:

> Data on Canada's exports to the United States, which are compiled from U.S. import data sources, are overstated as they include shipments to third countries via the United States often referred to as transshipment. As a result, Canada's exports to the rest of the world are correspondingly understated. (Canada 2003a, ch. 1, fn. 2)

NAFTA@10 describes an effort to reconcile the effect of transshipments on overall trade patterns (Canada 2003b, 61). The estimate identified is 1.2 percentage points. However; the possible underrepresentation does not stop at transshipments. As I note later, trade is increasingly a matter of intra-corporate trade in goods. And in the manufacturing sector, goods are assembled in a series of back-and-forth border assemblies between related and unrelated companies. Customs officials, however, count the good as an import on each entry in its entirety and not just with respect to the value-added from the previous crossing. As a result of both the counting of transshipments and cross-border assembly, bilateral trade is overrepresented and misallocated, with estimates of that representation ranging as high as 5 percent of Canada's trade with the U.S.

Table 1a: *Top Five Destinations for Canadian Direct Investment Abroad (Stocks), 2004*

Rank	**Country**	**% of Canadian Direct Investment Abroad**
1	United States	43.6
2	United Kingdom	9.9
3	Barbados	6.9
4	Ireland	4.6
5	Bermuda	2.6

Total Canadian Direct Investment Abroad (Stocks) = $445 billion

Table 1b: *Top Five Sources of Foreign Direct Investment in Canada (Stocks), 2004*

Rank	**Country**	**% of Foreign Direct Investment in Canada**
1	United States	65.1
2	United Kingdom	8.1
3	France	7.6
4	Netherlands	4.0
5	Japan	2.9

Total Canadian Direct Investment in Canada (Stocks) = $366 billion

Sources: Department of Foreign Affairs and International Trade, author's calculations.

eral years.[8] The size ranges from a high of over 90 percent of Ontario's trade with the United States to a low of 59 percent for Saskatchewan (Courchene 2002). But as *NAFTA@10* concludes, "Canada now exports more manufacturing to the U.S. than it consumes domestically." Canada is an open economy with significant trade (*NAFTA@10* estimates that C$1.9 billion of goods and services cross the Canada-U.S. border every day (Canada 2003b, 3)) and investment flows. But that openness is heavily tilted towards the United States.

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[8] A significant debate has taken place quietly about the impact of trade flows and whether the border matters. As early as 1996, Greg Ip wrote in the *Globe and Mail* that trade was increasingly being reoriented in a North-South direction at the expense of east-west trade. Ip said that almost all provinces ...

What is less apparent from these aggregate statistics is the changed structure of production that has accompanied these flows and that reinforces the growing economic integration between the United States and Canada. There is now a large body of literature that describes and accounts for the cross-border production structure that has emerged with the growing trade and investment flows. Increasingly, production in North America and globally, as well, has fundamentally altered the character of trade. In the years and decades after World War II trade was largely arms-length among independent companies in a variety of countries. But by the 1970s, the composition and character of trade began to change. Trade has been altered fundamentally, as described by Michael Hart and Bill Dymond, former Canadian trade negotiators:

> The evolution of international trade rules, in particular their extension to a growing range of public policies hitherto the exclusive preserve of domestic governance, reflects fundamental changes in the nature of the global economy. The old model of international trade involved inter-industry, arms-length exchanges of goods between autonomous firms operating from behind national borders. The new model of international exchange is characterized by intra-industry transactions, the increasing importance of trade in intermediate inputs, and the growing share of global business taking place on an intra-firm, intra-network, or other interrelated corporate basis. ...In the new, global economy, trade agreements address not only the relation-

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footnote 8 cont'd

exported more to the United States than they exported to other provinces (Ip 1996, 1). The Ip article was a journalistic foray into a discussion begun by a number of academics in what I have called the "border matters debate." John Helliwell and John McCallum (before he went off to politics) focused on the continuing impact that the border had on trade flows in North America. As McCallum noted in early analyses, the provinces traded 14 times more with each other than they did with states of comparable size and distance. What was less well reported was the fact that the ratio had declined from 20-to-1, even by the time of the "border matters debate" (McCallum and Helliwell 1994, 44-48; McCallum 1995, 615-619; and Helliwell 1996, 507-516). A later piece by Helliwell for the Brookings Institution in Washington, D.C. said that the border effect had been reduced to 12:1 by 1996 (Helliwell 1998).

> ship between nation states, but also the investment interests of TNCs, as well as the governance of related domestic economic policies. (Hart and Dymond 2002, 131)

Economists stopped talking about traded and non-traded goods and services. They stopped characterizing trade in classic arms-length flows. In fact, in current Canada-U.S. trade, "over 40 percent of U.S. trade with Canada is intra-firm — trade occurring between parts of the same firm operating on both sides of the border. The automotive industry is a prime example of the integration of production in North America. Every vehicle assembled in North America now contains nearly US$1,250 of Canadian-made parts" (Canada 2003b, 13).

Current and former politicians have not been quick to grasp the close relationship of trade and investment in the cross-border relationship, let alone in the larger global trading system. Canadian politicians face some very tough political decisions. Even as sophisticated a politician as former Alberta Premier Peter Lougheed has attempted to avoid the trade-investment nexus. In an effort urging the then-prime minister to create a closer collaboration with the United States, Lougheed wrote:

> Make no mistake: Foreign ownership is a legitimate issue. It is, however, a separate issue from free trade, which aims to build stronger economic ties between both countries. (Lougheed 2004, A19)

But today investment protection is a central issue in trade agreements. In the architecture of production, trade, and investment, FDI has become the principal pathway of exchange for the global trading system as opposed to the earlier and formative pattern of trade. While FDI may not lead to a buy-out of Canadian companies and the loss of Canadian ownership, there is little doubt that investment is a foundation of global trade. What is true for the global system is even more dramatically the case for cross-border exchange particularly between Canada and the United States but also between the United Sates and Mexico. Trade and investment are now considered complements to each other, rather than substitutes (OECD 2003). The reality is that investment and investment protection is as central a feature in deeper integration as trade was in the past.

As Barry Appleton writes in his chapter in this volume, "Investment agreements form the bedrock of international economic relations and as such they reside at the heart of the globalization debate." In fact, the breadth of critique and opposition to investment protection pursuant to Chapter 11 represents and heralds a debate more about loss of sovereignty and the threats to national autonomy through the forces of globalization than it does about the procedural and substantive matters in the investment chapter.

The Chapter 11 debate should be seen in a broader context of debate and dispute that have swirled around trade and investment in Canada, the United States, North America, and beyond. The battlegrounds are extensive.

This volume is one of the C.D. Howe Institute's *Border Paper* series. In the inaugural piece Wendy Dobson (2002) discusses the challenge to Canada's productivity and prosperity that current barriers between Canada and the United States have created. These obstacles were evident before September 11, 2001, but the terrorist attack and U.S. efforts to respond to future threats exacerbated the challenges to Canada's living standards and its economic position. Whether Canada and the United States take action to overcome the barriers and to move to deeper integration have become matters of some debate, at least in Canada. In the United States, meanwhile, in the midst of soaring trade deficits with China, anemic job creation and large and increasing budget deficits, trade and investment are subject to political critique and attack. Free trade generally, and NAFTA in particular, became much-maligned notions among the various political challengers to George W. Bush in the last presidential election. U.S. politicians have rushed to the microphones to declare their opposition to the original NAFTA, or any number of so-called free trade agreements that have been signed since NAFTA.

Not only that, the trade and investment debate is also raised in the regional and multilateral contexts. The investment protection debate is a serious issue in the regional free trade discussions, as well, most notably in the FTAA and in the WTO. In the former, then Canadian Minister of International Trade Pierre Pettigrew raised concern over supporting an investor-state dispute settlement procedure during the investment discussions on the FTAA. While permitting a dispute settlement procedure in recent Canadian bilateral accords, such as that with Chile, Canada has shown reticence in extending investment protection to the entire Western Hemisphere, excluding Cuba. Meanwhile, the United States incorporated investment protections, including investor-state dispute settlement procedures, for its Central American Free Trade Agreement (CAFTA) and bilateral accords, including those with Chile and Singapore, though not in the U.S.-Australia Free Trade Agreement as noted earlier.

In the multilateral context, investment has been a contentious issue in the Doha Development Round — at the WTO. Even though investment had been identified as a possible issue for negotiation for several years, including investment in the negotiation was continually opposed by member countries such as India. Civil society global interests, expressed largely in the streets in various meetings from Genoa to Miami, voiced heated opposition to the negotiation of a new multilateral investment agreement.

These civil society groups have opposed investment protection in their wide-ranging opposition to many aspects of the Doha Development Round. In the September 2003 ministerial session in Cancun, Mexico, investment once again failed to gain member-country support for inclusion in the negotiating round. The opposition to investment protections has thus migrated across the spectrum from the bilateral and cross-border discussions with the United States to the multilateral and larger examination of Canada's role in world. Directly or indirectly the investment protection debate is part of the regional versus multilateral debate and it is raised in the yet unanswered debate about the leading role that Canada plays or might play in a multilateral institutional setting, especially in the WTO and G-8. As a result, the Chapter 11 debate has become a part of larger, wide-ranging discussions and inquiries. I now turn to an examination of the chapters in this volume.

The Micro Aspects of Chapter 11

The first section of this volume examines the micro aspects of Chapter 11. This analysis focuses on investment protections prescribed by Chapter 11 itself. Much of the micro debate consists of a legal analysis of the procedural, substantive, and consequential aspects of the NAFTA investment chapter. It is, however, also a policy discussion. The policy debate emerges partly out of the legal analysis, though it is also concerned with the larger impact of the legal cases and their claims on government actions, especially government freedom of action. For instance, a variety of civil society groups, notably environmental ones, allege that the investor protection provisions safeguard corporations and their investments in Canada through Chapter 11. In addition these groups raise concerns that governments in Canada at all levels are restrained from taking legitimate action because of investors' threats to begin an investor-state action pursuant to Chapter 11 NAFTA.

As noted, the criticisms directed towards Chapter 11 investment protection have become louder and more pointed, without sacrificing their more wide-ranging aspects. Criticisms include at least the following major issues:

- The investment protections offered to foreign investors under Chapter 11 are unique. In Canada and, more recently, in the United States critics have argued that they provide protections to foreign investors that have been denied to domestic ones;
- Chapter 11 tramples on Canada's sovereignty in a variety of significant and harmful ways. The most significant criticism is that Chapter 11 imposes a regulatory chill on the Canadian government. Officials, according to proponents of this view, are reluctant to undertake environmental policies, for instance, out of fear that investors will claim that such policies have taken away their investment. As well, there have been charges that investor protection provisions threaten the continuance of the public provision of a variety of services, including such critical ones as health and educational services;

- There are many procedural criticisms raised by those concerned over the scope of the investor protection provisions of Chapter 11. Perhaps the most persistent is the alleged lack of transparency. The procedural provisions in Chapter 11 are built on the foundation of private arbitration protections. As a result, there are limits to the public's right to examine such elements as the legal documents, evidence in the cases, attendance at the hearings, or interventions from third parties. Government responses to the international tribunal determinations on liability and damages further fuel the debate. The Mexican government sought judicial reviews of the tribunal decisions in both the *Metalclad* and *Feldman* cases.[9] The Canadian government has sought judicial review in the *S.D. Meyers* decision. Broadly, governments have argued that these tribunals have overstepped their authority and rendered excessively broad interpretations, and in doing so legitimate public policy objectives could be thwarted; and
- There are also complaints over the substantive provisions of Chapter 11 investor protections. In this area, the criticisms include at least the national treatment provisions, the minimum standard of treatment provisions, and the expropriation provisions of Chapter 11. For each of these provisions, arguments have been raised over the scope and meaning of each protection.

The first chapters of this section review the major Chapter 11 cases, including all those against the Government of Canada. Barry Appleton tackles up front the critical Chapter 11 cases (he led, and continues to lead, a legal team for the investor and the investment in a number of these Chapter 11 disputes). In addition, Barry looks at the two specific substantive issues: expropriation and the minimum standard of treatment; as well, he explores the issues and the debate over transparency. Milos Barutciski of Davies Ward Phillips & Vineberg reacts in part to Mr. Appleton's conference presentation and further adds a gloss on these same issues.

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[9] For a listing of the complaints referred to in this publication, please see Table 1 at the end of this volume.

Barry Appleton's presentation supports generally the investor protection provisions and their application through the investor-state arbitration tribunals. Investor protection provisions, in his view, are "far from a new development in international law." The tribunals in the various cases — and in the Canadian cases in particular — have, in his view, zeroed in on arbitrary and discriminatory official behaviour and found the Canadian government in breach when such behaviour has been found. On the scope of expropriation, though he describes the various approaches to defining the process, he suggests that the tribunals all rely on a deprivation that is substantial or significant, underlining the customary international law understanding of expropriation. While Milos Barutciski recognizes that tribunal decisions have generally adopted a conservative approach to the scope of expropriation, he does suggest that the *Metalclad* decision may leave open the prospect of a wider scope for such action. He argues that the tribunal may have focused on interference with some of the attributes of property rights as opposed to the notion of "deprivation" of the totality of property rights. In a similar vein, Mr. Barutciski also raises some concerns over the full scope of "investment" as defined by Article 1139 and given expression by the *Pope & Talbot* tribunal. An overly broad interpretation of investment that possibly overlaps regulatory rights and licences, and a liberal interpretation of expropriation as in the *Metalclad* tribunal's examination, according to him, could arguably provide new ground in the determination of the process.

On MST, Barry Appleton notes the possible distinction between international and customary international law that is at the heart of the Free Trade Commission's *Interpretive Note*. Nevertheless, as Mr. Appleton says, MST, whether defined as international law or customary international law, still encompasses "fair and equitable" and full protection and security treatment, and recognizes that tribunals have determined that MST represents protections of foreign investment that are reasonable under the circumstances. Milos Barutciski also identifies how tribunals have focused on arbitrary or capricious behaviour. He goes on to raise some implications and further questions that the *Interpretive Note* has posed.

Transparency represents a number of serious questions in the administration of Chapter 11, as well as challenging the scope of international law. On the administrative side, Milos Barutciski observes that the *Interpretive Note* has addressed what has been an uneven disclosure of documents to the public. As he points out, many of the procedural aspects have been left to the tribunals, which explains some of the uneven release of information to the public. He notes that there is little basis for limiting the release of documents to the public. Mr. Barutciski also addresses the adequacy or appropriateness of addressing appeals or reviews with domestic courts. The concern was heightened following the decision by Mr. Justice Tysoe of the British Columbia court. However, two more recent dismissals of judicial review applications in Ontario have eased some fears. Ian Laird in his chapter in this volume most directly examines these questions. But Milos Barutciski leaves open the issue of whether a review process needs to be constructed either through a quasi-permanent Chapter 11 appellate body or a multilateral appellate body for matters of international law, housed possibly with the International Centre for Settlement of Investment Disputes (ICSID). Barry Appleton examines the concept of transparency in international law. Mr. Appleton argues for the importance of transparency as an element of fairness in international law. The *Metalclad* tribunal argued that transparency was an essential obligation of international economic law within MST of Chapter 11. Controversy has followed the decision of Mr. Justice Tysoe in his judicial review decision and his explicit rejection of transparency as part of Article 1105. The question of transparency will likely be examined again in a future tribunal.

Barry Appleton in the concluding section of his chapter undertakes a review of the many criticisms raised by opponents of Chapter 11. This section, which gives the title to his chapter, is a review of what he describes as "fact and fiction" in the Chapter 11 discussion. In this wide-ranging review Mr. Appleton tackles many of the strongest Chapter 11 challenges including whether:

- These tribunals can overturn domestic laws of the NAFTA parties;

- NAFTA gives foreign investors more rights than domestic ones;
- The investor protection provisions have opened a rash of claims, including frivolous ones;
- Chapter 11 limits the ability of governments to regulate in such critical service areas as health and the environment;
- Chapter 11 is transparent and accountable enough to the NAFTA publics; and
- Chapter 11 can restrict government sovereignty and fail to respect law and democracy.

This last issue is an opening view expressed by Professor Stephen Clarkson of the University of Toronto. A major critic of NAFTA generally and the investor-state Chapter 11 provisions in particular, his "Hijacking the Canadian Constitution" chapter chronicles many civil-society criticisms. On Chapter 11 he describes a number of problems specifically linked to investor-state protection, including:

- Transparency;
- Fairness, particularly because of the exclusion or the limitation on third-party participation;
- The bias of tribunals where the experts are focused on international law and there is a built-in selection bias against Canadians;
- The inclusion of a foreign element in the sphere of public law, specifically expropriation;
- The inclusion of damage awards in the investor-protection dispute settlement procedures, as opposed to the state-to-state dispute settlement arrangements, such as under Chapter 20;
- A statutory environment where governments are reluctant to act in the face of Chapter 11 litigation;
- The limited right of judicial review's undermining domestic legal examination and, in his view, subverting the most fundamental notions of justice and leading to the prospect, as occurred in the *Metalclad* decision, where a foreign domestic court, in this case a British Columbia court, is assessing the

adequacy of a public policy action or actions, in this instance the actions of various Mexican governments; and

- The extension of rights to foreign investors without corresponding obligations to act in the public interest.

Professor Clarkson makes a rather more unique contribution in his chapter in this volume when he looks at the impact of NAFTA generally on Canada. From his perspective, NAFTA's establishment of new and comprehensive disciplines that demand adherence by the NAFTA parties, have imposed an external constitution. This constitution restricts Canadian sovereignty and has several serious implications for the nation and its citizens.

- The constitution is an international agreement prohibiting Canada from exempting itself from international law even where it challenges a Canadian constitutional norm;
- There are inadequate institutions to accompany this external constitution, giving each country a veto over common business and limits on domestic institutions. In addition, there are positive obligations in such areas as intellectual property where NAFTA parties must conform to international NAFTA norms. Proscriptions apply whether Canadian legislatures agree or not, and act or not;
- While there is a formal right of abrogation, the actual changes to laws and management and business practice make it all but impossible to act. As Professor Clarkson says, "the potential impact of a breakdown in trade relationships with the United States would devastate the Canadian economy…"; and
- This constitution effectively extends rights only to corporations and individuals that can claim foreign investor or foreign investment status.

Cumulatively Canadian sovereignty has been significantly impaired according to Professor Clarkson. Canadians and their governments are now subject to foreign intrusion, including norms, rights, and restraints that Canadians never agreed to, though they have great influence over the economic protections and public policy actions of Canadians.

A Canadian Trade and Investment Policy

As noted in the foreword, we were fortunate in having the then-Minister of International Trade, the Honourable Pierre Pettigrew, attend at the university and deliver specific remarks on the theme of the May conference and the book. In addition, the Director of the Investment Trade Policy Division of DFAIT, as it then was, Stephen Brereton attended and spoke at the conference and provided a chapter for this volume. Professor Gilbert Winham, a noted trade policy expert from Dalhousie University, acted as a discussant for the Brereton presentation at the May conference and provides a chapter for this volume. As well, Ian Laird, an international trade lawyer, examines the impact of Canadian government policy and actions over investor complaints pursuant to investor-state provisions of Chapter 11.

The minister's presentation is a wide-ranging analysis and defence of Canadian trade and investment policy. Both the minister's and the director's papers support the recent investment initiatives of the Government of Canada and specifically the investment protection provisions of NAFTA Chapter 11. Both strongly defend Canada's support for such provisions on the classic grounds that:

- Such agreements provide added transparency, non-discrimination protections for Canadian investors, and a minimum international standard of protection in areas where Canadians consider foreign investment, and dispute settlement procedures for the Canadian investor. With Canadians investing more abroad than others invest in Canada, such protections provide, according to Stephen Brereton, a "greater measure of security for Canadian investors through assurances that national policies will not be changed unduly or applied in a discriminatory manner," and
- Canada has long been a supporter of a rules-based, rather than a power-based, approach to international trade and investment.

Not surprisingly both officials speak approvingly of the commission's *Interpretive Note*. As the minister stresses in his speech:

> I want investors' rights to be clearly stated and agreed upon and I want them to be properly interpreted....It is equally important that the ability of governments to regulate in the public interest not be compromised by unintended interpretations of investment rules.

The minister implies here, and states elsewhere, that tribunals have made errors and that, as a result, the NAFTA parties have found it necessary to take steps — the *Interpretive Note* — to insure that "...tribunals interpret Chapter 11 as its drafters intended " (Pettigrew 2001).

Ian Laird, in his chapter, speaks to the federal government's behaviour and policy, as well as its approving statements, suggesting that Chapter 11 disputes are a "source of irritation" for Canadian officials. That irritation has driven the government to clarify and re-clarify the balance between private interests and public purpose, in Mr. Laird's view. Further, he argues that the effort by the Canadian government and other NAFTA parties appeases certain U.S. interests and Canadian antiglobalization interests. The NAFTA parties have, through their interpretive efforts, in fact, undermined the rule of law which, from Ian's point of view, is particularly egregious for a "middle power" like Canada. But Canada's undermining of the rule of law goes further by supporting and launching its own judicial reviews in Canadian courts. according to Mr. Laird, the Canadian government has shown little respect for these international tribunals by, among other things, arguing for a low standard of review for the decisions of these tribunals.

Professor Gilbert Winham examines two issues. The first is an analysis of how extensive private rights are in the face of the government's public purpose. In part relying on the preliminary decisions of the tribunal in the *Ethyl* case, Professor Winham makes clear that investment protections extend to any law that has provisions that affect foreign investment, except for those excluded by the Annexes. The second issue addressed by Professor Winham is the matter raised by Minister Pettigrew and Director Stephen Brereton — that mistakes have been made in Chapter 11 and should be addressed by the NAFTA parties. Professor Winham looks at the judicial review decisions and whether a formal review process is required. While he appears to support an appeal process to possibly eliminate the variability in some of the early decisions, he is concerned about the use of national courts by the various governments to review tribunal decisions. The appeal to national courts, in his opinion, will greatly diminish the guarantees of investor protection. As serious, in his view, is the recourse to national courts by Canada. He strongly echoes the view of some others in this volume that Canada, as a middle power, may well not benefit from such a legal approach: "This could neutralize and render ineffective an internationalized dispute settlement mechanism."

Multilateral Trade and Investment Policy — The Macro Issues

The final area of inquiry concerns the extension of multilateral investment protections. This part examines efforts to extend investment protections multilaterally, as well as regionally and bilaterally.

John Hancock tries to understand why investment has become such a contentious issue in the organization of the global trading system. His analysis returns us to the changed architecture of international economics. As Hancock acknowledges, investment has become the key driver of international economic integration and the main basis of exchange in the global trading system, as global supply production by multinational corporations drives global trade.[10] Mr. Hancock chronicles in some detail the development of investment protections from BITs, through the current multilateral investment protections from services (General Agreement on Trade in Services), intellectual property (trade-related aspects of intellectual property rights (TRIPS)), trade-related investment measures (TRIMS), and investment measures in the Agreement on Subsidies and Countervailing Measures. While a comprehensive multilateral agreement on investment is now available in the Doha Development Round the question remains as to whether a multilateral investment agreement is ultimately required. John Hancock describes the global trading pressures that have brought investment protection to the multilateral negotiating table. He appears to describe an environment where markets at the commanding heights of the international economy will lead either to a much more comprehensive multilateral investment agreement or generate an ever more complex system of bilateral and regional investment agreements. Lou Pauly explores how we might get from here to there. Are global investment rules a consequence of market driven forces or do they remain very much the product of deliberate national cost-benefit analysis? If it is fewer markets and more deliberate national decisionmaking, then a realist perspective suggests that multilateral rules will await the appropriate political agreement. When the political moment arrives, according to Professor Pauly, we will likely see the trading of market access for guarantees of foreign direct investment. When will that political moment arrive? That also is hard to determine. It is the stuff of another volume on investment protection.

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[10] In UNCTAD's World Investment Report, the following describes the central driver of global investment:

> The fundamental economic forces driving growth remain largely unchanged. Intense competition continues to force TNCs to invest in new markets and to seek access to low-cost resources and factors of production. (UN 2003, 11).

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Deliberations on the NAFTA Decade:
Confronting Facts and Fiction in Light of Recent NAFTA Decisions

Barry Appleton

The heated debate surrounding the North American Free Trade Agreement (NAFTA) shows few signs of cooling. After weathering more than ten years of public debate and ten years of operation, this agreement continues to arouse controversy. A decade ago the focus of debate was on opening the U.S. economy to foreign goods and services. Today, the discussion has shifted to the scope of international investment protections in NAFTA and other investment agreements.

The central debate concerning agreements entered into by sovereign governments is whether those agreements that govern the treatment of foreign investors should be limited in any way and whether such agreements treat foreigners better than local citizens. Of particular interest is the investor-state arbitration process that allows individual investors to have their claims decided by impartial panels if governments fail to abide by the terms of these agreements. After years of NAFTA operations, a number of decided NAFTA disputes can shed some light on these questions. Looking at how these NAFTA obligations have been considered by decisions of NAFTA tribunals allows for some perspective on the issues raised in this most recent NAFTA debate.

The Purpose of Investment Agreements

Investment agreements form the bedrock of international economic relations and as such they reside at the heart of the globalization debate. Increased foreign investment is sought by countries for the resulting tangible enhancements in social and economic conditions. Today, new foreign investment is competitively sought by countries that compete on the basis of the quality of their domestic legal environments which encourage and respect basic legal rights and freedoms.

The decision to invest abroad is never easy. Investors carefully assess the political stability and the public governance conditions in countries where they consider investing. A virtual plethora of developing countries seek new investment agreements with developed countries because the very existence of such agreements can significantly impact the decision making process of foreign investors. The existence of these investment agreements not only provides reassurance to investors about specific investments, but it reflects the public affirmation of governments to fair and transparent governance in their economies. International investment agreements manage expectations of investors and governments alike. Domestic and foreign investors seek opportunities to participate in a transparent rules-based economic environment. Signatories to international investment treaties undertake to follow prescribed obligations and apply them in a fair and transparent manner. Business ventures are sought by foreign investors who are prepared to assume the same domestic business risks within a country as the local market participants, but they are not prepared to assume additional risks simply because they are foreign. Investors expect local economic environments to be transparent and free from corruption and bias. Foreign investors expect to have sufficient information to appreciate if they are being treated like others. This basic concept can be described as "legal security."

Legal security and good governance are even more important in a world where information virtually catapults around the world in seconds. With greater access to information comes a better ability for foreign investors to appreciate if government policies are pandering to local interests in an unfair way. Forever gone are the days when government officials could espouse one view locally and another abroad. Local speeches and press releases are now viewed at the same time by one public — whether located at home or abroad. This greater transparency results in greater scrutiny and hopefully better public policy.

The NAFTA Investment Regime

By forming NAFTA, Canada, the United States, and Mexico entered into a good governance covenant. NAFTA Chapter 11 contains a set of investment goals adopted by each of the three NAFTA countries and a process to settle investment disputes. Investment was seen to be the cornerstone of the new NAFTA economy and six pillars of the NAFTA good governance regime were designed to support this regime. The pillars supported policies to support transparency, fairness, and due process. They established:

- guarantees of non-discriminatory treatment;
- a commitment to provide the best in-country treatment to NAFTA investors;
- a commitment to act in a fair and transparent manner in accordance with international law and fundamental due process considerations;
- a prohibition against policies that link investments to local content rules, exchange controls, or other performance requirements;
- an agreement to permit capital flows in freely convertible currency; and
- compensation for expropriated investments.

The NAFTA drafters were not prepared to rely solely upon government aspirations as the basis for the NAFTA economy. In an attempt to ensure that governments adhered to the good governance covenant, NAFTA provided an enforcement mechanism that was accessible by those directly affected by unfair or discriminatory governmental activity, a process known as investor-state arbitration.

The NAFTA Disputes

Investor-state dispute settlement is far from a new development in international law. For more than 200 years, international treaties have established claims commissions with the powers to hear disputes between foreign investors and foreign state governments. For example, the *Jay Treaty* of 1794 not only established the peace terms at the end of the U.S. revolutionary war but it also established early investor-state tribunals to resolve disputes between British citizens and the newly-independent United States government in a de-politicized fashion.

More recently, the use of arbitration to settle investment disputes against foreign governments has been a central element of American and Canadian foreign policy and American bilateral investment treaties (BITs). In fact, the World Bank's International Centre for the Settlement of Investment Disputes (ICSID) reports that as of 1998, over 1,800 bilateral investment treaties were in force in the world. Today the number has grown to some 2,300 agreements. The vast majority of these BITs contain an investor-state arbitration clause. The goal of these agreements is to remove investment disputes from the realm of politically charged courts or international diplomacy, and to move them to a rules-based neutral process.

When NAFTA came into force in 1994, investor-state arbitration was not a novel approach to the settlement of international disputes. This form of dispute resolution had been used in nearly 75 cases under the ICSID and it had formed the basis for settlement of over 10,000 claims before the U.S.-Iran Claims Tribunal. What was new was the fact that NAFTA created a linkage, for the first time, between developed economies to use investor-state arbitration.

For a regional economy that generates over US$800 billion annually in trilateral trade, the area has seen surprisingly few claims proceed to NAFTA dispute settlement. As of January 2002, only one dozen NAFTA claims were raised against the three NAFTA governments.[1] Of these cases, three have been completed respecting Mexico, and another three have been substantially completed with respect to Canada. None of the cases against the United States had received a tribunal decision on the merits.

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[1] The claims against the Government of Canada were: *Ethyl Corp., S.D. Myers, Pope & Talbot*, and *UPS*. The claims against the U.S. government were *Loewen Group, Mondev, ADF*, and *Methanex*. Claims against the Government of Mexico were *Azinian, Metalclad, Waste*, and *Feldman*. In addition, there have been notices of intent filed by NAFTA investors but as of May 2002 they had not ripened into NAFTA claims. For a list through 2004, see Table 1 in the Conclusion section of this volume.

Ethyl Corporation and the Government of Canada

The *Ethyl Corporation* claim was the first NAFTA investor-state claim to proceed to arbitration.[2] The claim concerned a Canadian import ban on the chemical MMT, a compound used to replace lead as an octane enhancer for gasoline. The entire world supply of the additive was manufactured in Louisiana by Ethyl Corporation of Richmond, Virginia. MMT supplied by Ethyl Corporation has been used in nearly every gallon of Canadian gasoline since Canada removed lead from gasoline in 1979.

In 1996, the Government of Canada passed the MMT Act that imposed import bans on certain manganese substances and covered only one chemical, MMT. Under Canadian law, the Canadian government had the power to prohibit the sale of a product if it was considered harmful to public health or safety. Four independent bodies assessed the public safety of MMT over a 20-year period. None of them concluded that the use of MMT constituted a public health or environmental risk. Canada could not use its existing public policy powers to ban the use of MMT in Canadian gasoline as the record indicated no public health or safety risk.

Canada's *MMT Act* did not ban the use of MMT or its sale and manufacture in Canada. It required the American manufacturer to set up a plant in each and every Canadian province in which it intended to sell its gasoline additive. At the time this policy was under consideration, Canada's trade minister wrote a letter to Canada's environment minister attempting to dissuade him from enacting the MMT ban because no environmental basis supported it and because, in his department's assessment, the ban could violate Canada's international trade obligations, including those regarding expropriation.

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[2] *Ethyl Corporation v Canada*, Statement of Claim, October 2, 1997.

Evidence of the discriminatory intent could be seen in public statements made by government officials. After drafting the ban, the Canadian Deputy Prime Minister made public statements confirming that the rationale behind Canada's MMT ban was the desire to sell Canadian manufactured ethanol made from Canadian-farmed corn as a substitute for American-made MMT. She stated, "When we are talking about banning MMT and replacing it, we are talking about a variety of substances being used in ways that all parts of this country can benefit instead of giving all of the money to an American firm" (Copps 1996).

Ethyl Corporation filed a NAFTA notice of intent after Canada's House of Commons passed the *MMT Act*. Before the act was passed by Canada's Senate, officials from Ethyl Corporation appeared before a parliamentary committee and offered to withdraw their looming NAFTA claim if Canada would follow the recommendation of an independent assessment made by the Royal Society of Canada. Canada refused Ethyl Corporation's offer and the Canadian Senate passed the *MMT Act*. Shortly thereafter Ethyl Corporation filed its formal NAFTA claim.

Ethyl Corporation raised three complaints: First, Canada's *MMT Act* constituted a thinly-veiled investment measure that compelled Ethyl Corporation to move manufacturing operations from the United States to Canada as a condition of selling its MMT product. Second, Canada's measure violated NAFTA's national treatment obligations by treating Canadian investments that manufactured MMT better than U.S. investments that made MMT. Third, the company alleged that Canada's export ban constituted a taking of Ethyl Corporation's long-standing Canadian market for its product.

Canada challenged the jurisdictional ability of Ethyl Corporation to bring a claim over these types of complaints under NAFTA. The NAFTA tribunal unanimously dismissed Canada's objections.[3] Ten days later, Canada settled the NAFTA claim, reimbursing the company for US$13 million in expenses, withdrawing the import ban, and issuing a public statement by two different ministers in the Canadian government confirming that there was no scientific, health, environmental, or public safety concerns with MMT. The government stated that "Current scientific information fails to demonstrate that MMT impairs the proper functioning of automotive on-board diagnostic systems ... and there is no new scientific evidence to modify the conclusions drawn by Health Canada in 1994 that MMT poses no health risk."

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[3] *Ethyl Corp.* Award of Jurisdiction, June 24, 1998.

While no final decision was made by the NAFTA tribunal, it is clear that Canada's behaviour regarding the creation of the MMT Act was not based on proof of risk and on its face appeared to violate several NAFTA obligations concerned with protection against discrimination and fairness.

S.D. Myers, Inc. and the Government of Canada

The *S.D. Myers, Inc.* NAFTA claim[4] arises out of a haphazard set of circumstances surrounding the remediation of polychlorinated biphenyl (PCB) wastes in Canada. S.D. Myers, Inc. was the leading environmental remediation firm dealing with the treatment of PCB wastes in electrical transformers in the United States. In 1989, Canada and the United States concluded a bilateral agreement on the processing of hazardous waste. Under this agreement, hazardous waste could be shipped for processing from Canada to the United States, provided that the U.S. Environmental Protection Agency (EPA) approved the transfer. Under U.S. environmental regulations, all PCB waste had to be destroyed within a set period of time. In Canada, there was no requirement to destroy PCB waste, only to store it.

In 1995, Canada had only one PCB waste destroyer, in Swan Hills, Alberta. While the majority of Canada's PCB wastes were located along the Canada-U.S. border between Quebec City and Windsor, provincial legislation prohibited the Swan Hills incinerator from destroying PCB waste generated outside Alberta.

In 1993, before the EPA approved the import of PCBs into Canada, S.D. Myers, Inc., an Ohio-based EPA-approved PCB waste remediator, established a Canadian affiliate to help it treat Canadian PCB wastes primarily located in Ontario and Quebec. S.D. Myers, Inc. was warmly received by Canadian entities holding PCBs because of its proximity to most of the Canadian PCB wastes — which reduced the risk of accidental PCB spills during transport — and because of the cost. While Canadian PCB destruction prices were set at monopolistic levels, the PCB costs offered by S.D. Myers were based on the market-driven U.S. rates, averaging half those of Canadian competitors.

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[4] *S.D. Myers v Canada*, Statement of Claim, October 30, 1998.

By 1996, there was little PCB waste left in Alberta and the Swan Hills facility sought new sources of PCB waste for destruction. In May 1996, the Alberta government permitted the Swan Hills facility to process PCB waste from outside Alberta. While Swan Hills took steps to obtain contracts in Canada, it could not acquire commitments from Canadian waste holders thanks to its high destruction costs. Instead, the Canadian holders were engaging in contracts with S.D. Myers, Inc. that could only come into force at such time as the U.S. EPA gave its permission to allow PCB imports into the U.S. This permission was anticipated imminently.

The Swan Hills facility changed its strategy from competing for market share against S.D. Myers to compelling Canadians to process their PCB wastes in Canada. Relying on the Basel Convention, which states that countries should try to destroy their own waste domestically, the Swan Hills facility hired an Ottawa lobbyist who had recently been the Chief Policy Advisor to Environment Minister, Sheila Copps. Canada had no environmental policy basis for this strategy, only domestic Canadian industrial policy considerations. Unfortunately for Canadian officials seeking to impose a ban on export, the Basel Convention contains a clause that specifically recognized the existing Canada-U.S. bilateral agreement. On a public policy basis, environmental remediation by U.S. companies under the Canada-U.S. agreement was fully compliant with the requirements of the Basel Convention.

In July 1996, the EPA permitted S.D. Myers and eventually 11 other EPA-approved facilities to treat PCB waste from Canada. The opening of the border posed a tremendous threat to the Canadian-based PCB environmental remediators because Canadian wastes would be processed in the United States and thus, would not be available for the Canadian companies. The documentary records showed that the most senior officials of the Canadian government were involved in secret meetings with lobbyists for the Canadian industry in order to protect the Canadian industry from the more competitive U.S. company, even if that meant increasing costs to consumers by over 100 percent.

When Canada learned that the EPA would open the border to the import of PCB waste, it issued an emergency environmental ban on exports of PCB wastes to the United States. Briefing material prepared at that time by Environment Canada indicated that officials within the department saw the emergency ban as a trade prohibition rather than as a sound environmental policy measure. Some officials opposed the greater transportation distances required for most Canadian PCBs before destruction in Northern Alberta. Similarly, other Canadian government departments opposed the emergency ban. On November 16, 1995, Environment Minister Sheila Copps announced the emergency ban, which lasted for 18 months. The regulations affecting the ban specifically stated that the ban resulted from the EPA's decision to permit S.D. Myers to import PCB waste from Canada for processing at EPA-approved facilities in the United States.

The effect of Canada's PCB export ban was immediate and devastating. While S.D. Myers had customer bids or orders on almost C$80 million of Canadian PCB wastes, the company was only able to process a few small orders while the Canadian border was open. The ban effectively destroyed S.D. Myers' Canadian business operations and seriously affected its U.S. business, which had been ramped up to cope with the Canadian orders. S.D. Myers was targeted not because it could not meet Canadian environmental rules, as it was capable of meeting all of these requirements. It was targeted because it was operated by American owners, its only offence.

In July 1998, S.D. Myers filed a Notice of Intent under NAFTA Chapter 11 against Canada. The company immediately sought neutral consultations with the Government of Canada, which were refused. After waiting fruitlessly for one year for consultations to take place, S.D. Myers filed its NAFTA claim in October 1998. The claim alleged that Canada's PCB Waste Export Ban constituted a discriminatory and unfair attack on S.D. Myers based on its U.S. nationality. In a series of unsuccessful motions, Canada attacked the jurisdiction of the NAFTA tribunal to hear this complaint. Canada lost each of these motions entirely.

In November 2000, the NAFTA tribunal issued its decision in favour of S.D. Myers Inc. The tribunal commented on the unfairness of Canada's ban that was designed to discriminate against S.D. Myers because it was American. After reviewing the evidence, the tribunal also concluded that there was no real environmental basis to Canada's policy — only a discriminatory trade purpose. The NAFTA tribunal commented on this trend when it stated:

> Insofar as intent is concerned, the documentary record as a whole clearly indicates that the Interim Order and the Final Order were intended primarily to protect the Canadian PCB disposal industry from U.S. competition. Canada produced no convincing witness testimony to rebut the thrust of the documentary evidence.
>
> *The tribunal finds that there was no legitimate environmental reason for introducing the ban.* [The tribunal noted that there were other equally effective means of encouraging the development and maintenance of a Canadian based PCBs remediation industry]. Insofar as there was an indirect environmental objective — to keep the Canadian industry strong in order to assure a continued disposal capability — it could have been achieved by other means.[5]
>
> The NAFTA parties properly wanted to ensure that Chapter 11 could not be used to impugn government measures that are protected by other specific aspects of the NAFTA ... Canada could have satisfied any health or environmental concerns it had in a manner that did not impair open trade. *As Canada implicitly agreed when it subsequently lifted the ban, it would have better served*

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[5] *S.D. Myers v Canada*, Partial Award, November 13, 2000, paras. 194-195. [Emphasis added.]

> *the cause of a safe environment if it had kept the Canadian border open, but put in place safeguards.*[6]

These words from the NAFTA tribunal were telling as Canada's environmental policy was not enhanced because of its protectionist environmental ban. This position was taken not only by the NAFTA tribunal, but also by leading Canadian environmental groups. Years after Canada closed its border to the destruction of PCB wastes, the problem of PCB wastes continues. In March 2002, the government of Ontario suggested ordering the destruction of PCBs in storage. Environmental groups immediately opposed this suggestion on the basis that transporting PCBs the long distance from Ontario to Swan Hills, Alberta for destruction would raise unacceptable transportation risks (Mittelstaedt 2002)[7] and they decried the lack of access to safe U.S. PCB remediation facilities that would have been closer than the Alberta option.

In January 2001, Canada initiated a domestic court review of the merits award in the S.D. Myers claim. This judicial review was a thinly-veiled attempt to appeal the NAFTA decision through claims of jurisdictional error. Canada's unprecedented application was a provocative and unusual step. In a well-reasoned decision in January 2004, the Federal Court of Canada dismissed Canada's judicial review and ordered costs against Canada. Canada paid

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[6] *S.D. Myers*, Partial Award, November 13, 2000, para. 298.

[7] The newspaper report included the following:

> ...A plan by the Ontario government to require the destruction of PCBs over the next three years is "ill-considered" and could lead to spills along highways in Ontario, Manitoba, Saskatchewan, and Alberta, a major environmental group warns. The group, the Pembina Institute, is urging Ontario's Environment Ministry to shelve a proposal made in December to require the destruction of the 100,000 tonnes of PCB wastes now held in storage around the province.
>
> Normally, environmentalists would applaud the destruction of PCBs, which cause cancer in animals and have been found to impair development in young children. But the institute says the province doesn't have the capacity to destroy the wastes and that Ontario PCB owners will be forced to move them to Alberta's Swan Hills hazardous waste incinerator, raising the possibility of spills from trucks along the way.

S.D. Myers nearly C$10 million in damages under the NAFTA award.

Pope & Talbot, Inc. and the Government of Canada

The controversy between Canada and the United States over softwood lumber has been a long-standing bilateral irritant. In 1996, the governments of Canada and the United States agreed to a Softwood Lumber Agreement (SLA) that established a voluntary export restraint regime on Canadian softwood lumber to the United States. At the time of its negotiation, it was clear that the terms of the agreement violated the trade in goods provisions of NAFTA, Chapter Three. Under the terms of NAFTA, while U.S. consumers and Canadian lumber workers suffered by this restraint regime, only the governments of Canada, the United States, or Mexico could challenge this violation. None of these governments raised any objection.

In 1997, Pope & Talbot, Inc. wrote to the government office administering the implementation of the Softwood Lumber Agreement in Canada enquiring about how its quota was determined. Pope & Talbot was concerned because it believed that the government's quota data was incorrect, so it wanted a better understanding of the quota calculation. In reply, the department informed Pope & Talbot that it applied a certain quota formula but it would not disclose specifically the basis for the quota's calculation.

Pope & Talbot launched a NAFTA investor-state claim over what it viewed as the fundamentally arbitrary and unfair manner in which Canada treated this American company which operated in Canada.[8] In its NAFTA claim, Pope & Talbot did not challenge the terms of the Softwood Lumber Agreement itself, rather it challenged how Canada's implementation of the regime violated the investment provisions under NAFTA Chapter 11. The Pope & Talbot claim challenged the fairness by which Canada's softwood lumber export quota regime handled new marketplace entrants, discretionary reserves issued by the Canadian minister, the information provided by non-quota participants who provided critical information and the application of special onerous export levies imposed on specific sub-regions of Canada that affected the company. In addition to the administrative issues, claims were raised about failures to provide national treatment and compensation for expropriation.

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[8] *Pope & Talbot v Canada*, Notice of Arbitration, March 25, 1999.

After launching its NAFTA claim, the government commenced an invasive audit of Pope & Talbot's operations. In the course of this investigation, termed by Canada a "verification review," Canada demanded that the investor transfer hundreds of thousands of pages of original financial data kept in its Portland, Oregon head office to its regional forestry office near the Rocky Mountains. The company objected and invited Canadian officials to see the documents at their Portland offices. At the same time, the investor asked Canada to identify the basis of its legal authority for the verification review.

Canada's Softwood Lumber Division (SLD) never disclosed any specific basis for its verification review, and at this time, its attitude towards the company turned belligerent. While it confirmed that the verification review was caused by the initiation of the NAFTA claim, the SLD maintained that the information sought was unconnected to the NAFTA case. When Pope & Talbot pressed the SLD to produce the basis of its lawful authority to review its records, the director of the SLD threatened to revoke the American company's softwood lumber quota entirely. When the company sought to have this threat reviewed by the Canadian minister of trade, the SLD official promised to pass along the company's comments. In reality, the official did not pass along materials from the company. Instead he informed the minister that the American company was breaking Canadian law. He also stated that Pope & Talbot's corporate officials should be arrested and detained by the Royal Canadian Mounted Police if they crossed the border.

The *Pope & Talbot* tribunal reviewed the process followed by Canada to implement its softwood lumber export control regime in Canada. In its careful review, the NAFTA tribunal concluded that Canada's decisions on how it implemented its export regime were reasonable in the circumstances.[9] When looking at whether a government program met the international law standard of treatment, the NAFTA tribunal was exceedingly deferential to the public policy choices made by the Canadian government, even when these choices were not equitable. For example, in relation to an onerous "super fee" imposed by Canada on a certain volume of lumber coming from a certain sub-section of British Columbia that disproportionately hurt Pope & Talbot's business, the tribunal stated:

> Canada might have chosen another approach to settlement, one that shared the burden more equitably across the range of B.C. producers that received the benefits of the stumpage reductions. However, it is not the place of this tribunal to substitute its judgment on the choice of solutions for Canada's, unless that choice can be found to be a denial of fair and equitable treatment. Given the large number of B.C. producers affected by the settlement as well as the hierarchical treatment of shipment levels under the SLA itself, the tribunal cannot conclude that Canada's decision to apportion the costs as it did was a denial of fair and equitable treatment to the investment.[10]

On these issues, the tribunal concluded that Canada had not violated its NAFTA obligations. At the same time, the tribunal did find that Canada violated international law standards of fairness in how it treated the American investor once it commenced its NAFTA claim. The NAFTA tribunal found that this conduct by Canada violated NAFTA's guarantee of treatment in accordance with international law. In its award on the merits, the NAFTA tribunal concluded that Canada's actions violated Canada's international law obligations in the treatment of Pope & Talbot by Canadian officials. This treatment caused the company to temporarily close its operations in Canada and the tribunal established Canada's responsibility to compensate Pope & Talbot for the harm arising from this shutdown. The words of the tribunal were scathing:

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[9] The tribunal reviewed the manner in which the quota regime handled new entrants, discretionary reserves, non-participants who provided critical information and special onerous export levies imposed on specific sub-regions of Canada. In the tribunal's opinion, all of these met the international law test. (*Pope & Talbot*, Award on the Merits, Phase 2, paras. 123, 125, 128, and 155).

[10] *Pope & Talbot*, Award on the Merits Phase 2, para. 155.

> The relations between the SLD and the investment during 1999 were more like combat than cooperative regulation, and the tribunal finds that the SLD bears the overwhelming responsibility for this state of affairs. It is not for the tribunal to discern the motivations behind the attitude of the SLD; however, the end result for the investment was *being subjected to threats, denied its reasonable requests for pertinent information, required to incur unnecessary expense and disruption in meeting SLD's requests for information, forced to expend legal fees and probably suffer a loss of reputation in government circles.* While administration, like legislation, can be likened to sausage making, this episode goes well beyond the glitches and innocent mistakes that may typify the process. *In its totality, the SLD's treatment of the investment during 1999 in relation to the verification review process is nothing less than a denial of the fair treatment required by NAFTA Article 1105,* and the tribunal finds Canada liable to the investor for the resultant damages.[11]

Canada was obliged to pay damages to Pope & Talbot as a result of this surprising and egregious behaviour.

The *Pope & Talbot* tribunal made other important procedural decisions dealing with fairness. In its Procedural Decision on claim of Cabinet confidentiality, the NAFTA tribunal rejected Canada's unspecified and extensive executive privilege claim over policy papers that allegedly disclosed discrimination or arbitrariness in the allocation of a quota regime to an American company operating in Canada. To suppress these incriminating documents, Canada relied on a certificate signed by the most senior government official in the country attesting to the fact that the documents requested were privileged under Canadian law. The certificate did not disclose the actual existence of the documents or provide any specific reasons why the documents were actually privileged. Similar secrecy provisions are unknown under Mexican or American law. The NAFTA tribunal ruled that this certificate did not have any application to an international arbitration and that Canada's use of this procedure could be a violation of the fairness and equality provisions incorporated into NAFTA through the United Nations Commission on International Trade Law (UNCITRAL) rules.[12]

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[11] *Pope & Talbot*, Award on the Merits Phase 2, para. 181. [Emphasis added.]

Finally, the *Pope & Talbot* tribunal made important observations on the contemporary meaning of the international law standard of treatment and Canada's attempt to lower this level of protection through an Interpretive Statement in the tribunal's award on Damages.[13]

The *Pope & Talbot* claim stands as a landmark case. It demonstrated that high-handed government behaviour would not be tolerated in developed economies. The tribunal's findings in favour of transparency, public access, and fair treatment will serve as important themes that no doubt will be followed by other international tribunals.

Metalclad Corporation and the Government of the United Mexican States

The *Metalclad* case focused on the reopening of a toxic waste facility in the Mexican town of San Luis Potosi. The American investor purchased a dilapidated existing toxic waste facility with a view to renovating the facility to meet Mexican environmental standards. The American company received the appropriate federal environmental authorizations required under Mexican law. When it planned to commence its renovations, it was met with a cease work order from the local municipality claiming that the U.S. company had not obtained a local permit. As a matter of Mexican domestic law, Metalclad's existing Mexican federal authorization would supersede all local requirements. The local government demanded that the company stop work immediately.

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[12] *Pope & Talbot*, Award on Crown Privilege and Solicitor-Client Privilege, September 6, 2000, para. 1.5.

[13] *Pope & Talbot*, Award on Damages, May 31, 2002.

The American company, after reviewing the situation with American diplomats in Mexico, decided to proceed with construction. When it was to open its newly renovated facility, the company was denied the opportunity to operate by the local town council. Shortly thereafter, the state governor, on his last day of elected office, designated the newly renovated Metalclad site to be part of a rare cacti preserve (despite the fact that there were no rare cacti in its vicinity), shutting down the entire operation without the payment of any compensation to the U.S. investor.

Metalclad brought a NAFTA claim based on violations of international law standards of treatment and expropriation.[14] The investor was successful in the merits phase of its arbitration as the tribunal found the Mexican local actions were unfair and discriminatory and the state action constituted an unlawful taking under international law and NAFTA.

In April 2000, the Government of Mexico sought a judicial review of the NAFTA tribunal award in the *Metalclad* case on the basis that the NAFTA tribunal operated outside its jurisdiction in making its decision. This claim before the Supreme Court of British Columbia resembled a rehearing of the case on the basis of legal error rather than a judicial review dealing with jurisdiction. The case was decided by a sole domestic court judge who was forced to develop a single expression of the content of international law,[15] a feat that has not yet been undertaken by the International Court of Justice. The Canadian reviewing court decided that the tribunal was essentially correct in its decision but that, in its opinion, there was no international law rule that required governments to publish laws before they became effective. As a result, the Canadian reviewing court reduced the Metalclad damage award by approximately US$1 million to US$15.5 million.

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[14] *Metalclad v United States of Mexico*, Notice of Intent, December 30, 1996.

[15] *United Mexican States v Metalclad Corporation*, 2001.

Azinian and the Government of the United Mexican States

The *Azinian*[16] case demonstrates that the NAFTA investor-state dispute process has the tools to differentiate between bona-fide and spurious claims. This case concerned a contract award by the municipality of Tijuana to an American company for the pick-up and processing of garbage. Under the terms of the contract, the U.S. company was to provide 60 new garbage trucks with staff to service Tijuana. Instead, the U.S. investor supplied two used vehicles and as a result it found its garbage contract terminated. The U.S. investor brought a claim against Mexico alleging an expropriation, discriminatory treatment on the basis of nationality, and a violation of international law. After hearing the claim, the NAFTA tribunal decided in favour of Mexico and dismissed the investor's claim.[17]

Loewen Group and the Government of the United States

The *Loewen claim*[18] focuses on one of the oldest concepts in international law: the requirement that courts give justice and fair treatment to foreigners that appear before them.

The facts are simple. Loewen Group, a Canadian funeral home chain, was taken to court in Mississippi over allegations by a local funeral home operation that Loewen engaged in unfair business practices. On a US$2.5 million lawsuit, the jury issued a US$500 million award. When Loewen sought to appeal the decision, the Mississippi appeals court requested that the company post a bond for US$625 million before it would review the case. Loewen Group could not post such a bond and was thus unable to appeal. It later settled the case by paying some US$175 million to the Mississippi funeral home. Shortly thereafter the Canadian company declared bankruptcy.

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[16] *Robert Azinian et al. v United Mexican States*, Notice of Intent, undated.

[17] *Azinian*, Final Award, November 1, 1999.

[18] The *Loewen Group, Inc. and Raymond L. Loewen v United States of America*, Notice of Arbitration/Statement of Claim, October 30, 1998, ICSID/NAFTA No. ARB (AF)/98/3.

Loewen based its NAFTA claim on what it described as the denial of justice it received from the Mississippi courts. In particular Loewen alleged that the trial judge and jury made discriminatory anti-Canadian remarks during the trial that rendered the process unfair and biased. In addition, Loewen alleged unfairness in the decision of the Mississippi appeals court to not permit a domestic court appeal without the posting of a US$625 million bond as security, a requirement that the court imposed strictly because Loewen was foreign to the State of Mississippi.

It is also useful to note that in October 1998 the former Governor of Mississippi wrote to the NAFTA tribunal stating that the Loewen trial "was tainted by xenophobic rhetoric that may have resulted in a violation of Loewen's due process rights." The governor also admitted that the decision of the Mississippi Court of Appeal to not reduce the appeal bond requirement denied Loewen a meaningful opportunity for review.

The tribunal concluded that while Loewen did suffer a denial of justice, due to technical flaws its claim could not succeed. It would appear that the Loewen tribunal did not create or extend any new legal obligation regarding the protection of investors against denial of justice. Loewen made the same type of claim that the Government of Canada was entitled to bring to the International Court of Justice on the same issues and for the same amount of compensation. At no time did NAFTA place new or additional obligations upon the U.S. government with respect to the judicial process.

Methanex and the Government of the United States

In August 2000, then California Governor Gray Davis expressed concerns over the use of a gasoline additive MethylTetrylButyl Ethenol (MTBE) in gasoline in his state. MTBE is a possible human carcinogen and is water-soluble. It had been found in water samples from Lake Tahoe and other locations throughout California.

MTBE is made from methanol which is a derivative of methane gas. Methanex, a Canadian methane and methanol company, was concerned about the governor's statements. Even though Methanex does not manufacture MTBE (only its upstream ingredient), the company initiated a NAFTA claim against the U.S. government for California's acts, which it alleged were discriminatory, unfair, and which constituted an act "tantamount to expropriation."[19] The company has claimed damages for the decrease in its share price caused by the Governor's statement, which it calculates to be approximately US$970 million.

The Methanex tribunal ruled that the investor was too far removed from the California measures as it did not actually make or sell MTBE.[20] The tribunal dismissed the vast majority of the claim. Only a very small part of this claim, regarding allegedly corrupt behaviour on the part of the Governor, is still before the tribunal.

It is premature to make conclusions about the outcome of the remaining part of the claim. It is important to note that the Methanex claim is as much about a failure to observe due process considerations by the State of California as it questions the nature of the state's regulation of MTBE. What is clear is that at no time does the Methanex claim purport to prevent California from taking steps to protect the health or safety of its citizens.

Addressing NAFTA Fictions

> *Waving 5,000 pages of trade agreements, Representative Robert Matsui, a California Democrat, argued that new treaties could affect federal laws on matters from food safety to monopolies. "Trade is no longer primarily about tariffs and quotas," he said. "It's about changing domestic laws." In the Senate, Massachusetts Democrat John Kerry wants to amend the bill to make it harder for companies to file claims.*

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[19] *Methanex Corporation v United States of America*, Statement of Claim, December 3, 1999.

[20] *Methanex*, Preliminary Award on Jurisdiction and Admissibility, August 7, 2002.

> *"NAFTA was never intended to infringe on U.S. sovereignty in such a way," he said. (Roosevelt 2002)*

The debate over the NAFTA investment chapter is not about international investment, but it is truly a debate over globalization itself. However, the debate over the NAFTA investment chapter is the continuation of the successful overturning of the Organisation for Economic Co-operation and Development's (OECD) proposed Multilateral Agreement on Investment in 1998 and the failure of the Seattle World Trade Organization (WTO) ministerial in 1999.

The NAFTA controversy, now focused on the investment chapter, resulted in the heated debate about the nature of future investment policy in Canada and the United States. Much of this debate has concerned the impact that NAFTA tribunal decisions could have upon government decisionmaking. For example, the Ecumenical Coalition for Economic Justice stated in their April 2001 newsletter under the heading "Protect the Environment: End investor-state suits,"

> ...The investor-state mechanism permits foreign investors to sue national governments for virtually any action that decreases their expected profits on the grounds that the measure is "tantamount to expropriation" of their assets. TNCs [trans-national corporations] have used this clause to challenge a variety of measures designed to protect human health and the environment. ...collectively these suits show a wide range of challenges to government regulatory powers. They are particularly disturbing because of their implications for denying governments the ability to safeguard human health and the environment. They also pose an enormous challenge to the democratic process by enabling corporations to veto national regulatory policies. (Ecumenical Coalition for Economic Justice 2001)

Even the *New York Times* has been caught up in this sensationalization of trade policy. In an article entitled "NAFTA's Powerful Little Secret," Anthony DePalma wrote:

> Their meetings are secret. Their members are generally unknown. The decisions they reach need not be fully disclosed.

> Yet the way a small group of international tribunals handles disputes between investors and foreign governments has led to national laws being revoked, justice systems questioned and environmental regulations challenged. And it is all in the name of protecting the rights of foreign investors under the North American Free Trade Agreement. (DePalma 2001)

In a vociferous debate, the NAFTA investment chapter is accused of adding new investor protections to help the business community overturn government regulation, of creating a new system of dispute resolution, and of eroding the sovereignty of democratically elected legislatures to make laws.[21] These are powerful accusations. However, are they well-grounded on the facts? In the light of the recent NAFTA decisions, it is possible to now separate the fictions from the facts.

Fiction #1: *NAFTA investor-state panels overturn domestic laws.*

Fact: *NAFTA investor-state tribunals have absolutely no power to overturn domestic laws and none have done so.*

- NAFTA investor-state tribunals do not have the power to overturn domestic laws. The agreement is very clear that the only remedy available to investors is compensation. NAFTA panels have much less authority than WTO panels, which can make policy recommendations to governments about changing laws. NAFTA panels can only decide whether a government has acted consistently or inconsistently with NAFTA.

- No NAFTA tribunal has ever overturned any government law or regulation. In the Metalclad claim, the Mexican municipal law prevailed (even though it violated domestic Mexican constitutional law), and in the S.D. Myers claim Canada withdrew its anti-American export ban well before the company ever started its NAFTA claim. In the Ethyl claim, Canada simply de-activated regulations that it admitted were without scientific basis and settled the case, with the NAFTA tribunal's making no final award on liability. There is no basis to the contention that NAFTA tribunals overturn laws made by democratically elected governments.

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[21] Steven Shrybman has written "to begin, it is important to understand that, prior to NAFTA, only national governments had standing to invoke dispute resolution processes under international trade agreements" (Shrybman 2001, 131). It is clear from the record that this statement is simply incorrect.

Fiction #2: *NAFTA investor-state arbitration is a revolution in international law.*

Fact: *Investor-state arbitration has existed for hundreds of years.*

- The investor-state dispute settlement mechanism has been used for hundreds of years. It is simply not a policy innovation brought in by NAFTA. The investor-state model has been used to settle thousands of disputes between governments and foreign citizens. In fact, the investor-state system was used to settle the disputes between revolutionary America and United Empire Loyalists that fled the United States for Canada during the U.S. Revolution.

- Investor-state arbitration has been widely used. It was used to deal with over 10,000 claims made by Americans for harm suffered from the Iranian revolution in 1979, and the ICSID has heard over 100 cases arising from bilateral investment treaties. This alternative dispute resolution method has long been accepted by countries to deal with disputes between individual citizens and countries. It simply is not accurate to say that it is a new process.

Fiction #3: *NAFTA investor-state arbitration gives foreigners more protections than U.S. investors.*

Fact: *NAFTA does not give foreigners more rights than U.S. investors.*

- NAFTA did not create powerful new investment rights. In fact, the NAFTA investment chapter did not create any new international law obligations. The areas of national treatment, most-favoured nation treatment, treatment in accordance with international law, transfers, and expropriation all relied upon established international law obligations that were derived from outside NAFTA. NAFTA used existing models of international dispute settlement between governments and individuals and pre-existing international law obligations.

- NAFTA was designed to encourage countries to treat their own citizens and foreign investors in an equal, transparent, and fair manner. The NAFTA investor-state decisions thus far demonstrate that Chapter 11 has been successful in ensuring that these obligations are observed by the signatory governments. The obligations of equality, transparency, and fairness are also present under domestic legal regimes where remedies ensure natural justice, equality, procedural, and substantive fairness to domestic citizens. The only difference is that international law recognizes that different countries will have differing thresholds of "fairness" standards and therefore establishes an international floor or standard below which treatment of foreign investors cannot go. The international standard attempts to secure international comity and predictability for foreigners abroad. Moreover, the argument that this international standard gives foreigners a higher level of treatment than domestic investors is simply incorrect because it is the wrong comparison. If they were to operate in another NAFTA country, those very same domestic investors would also be entitled to protections similar to those they would get at home.

- The international standards adopted in NAFTA, whether for labour, environmental, human rights, or investment issues, have been explicitly designed to encourage domestic governments to enhance their domestic regimes in order to create predictable and favourable conditions for trade and investment.

Fiction #4: *NAFTA has opened the floodgates to questionable claims.*

Fact: *There have been few NAFTA claims and frivolous NAFTA arbitrations have been dismissed.*

- Under NAFTA's investment chapter, any citizen or corporation in North America is eligible to bring a NAFTA investor-state claim. Thus over 300 million citizens and countless millions more corporations, non-profit groups, and associations are eligible to bring claims. Over a period of eight years, there have been fewer than 20 NAFTA claims brought by these hundreds of millions of potential claimants. Even in the world of P.T. Barnum, the mere dozen claims cannot be reasonably described as a flood. In fact, the only real surprise is how few claims have been made given the large pool of potential claimants in each NAFTA country.

- Non-meritorious NAFTA claims have been defeated. Two claims have been won by Mexico. Where claims have succeeded, the NAFTA tribunals have pointed to clear evidence of unfair or discriminatory behaviour that has been targeted against foreigners (in all of these cases, Americans) by officials in the Canadian or Mexican governments.

- A related concern raised by critics is that NAFTA investor-state claims are subjecting governments to billions of dollars in potential liability, which should not be allowed to happen. However, by examining the amount of compensation that has actually been paid out by NAFTA governments, it is immediately obvious that the impact on the public treasury has been exceedingly small. To date, NAFTA governments have paid out less than US$29 million since the NAFTA came into force over eight years ago. During this same period, nearly US$5.2 trillion of trilateral NAFTA zone trade has been transacted. The total amount of damages paid out under NAFTA Chapter 11 therefore represents a minuscule number that is less than one-thousandth of one percent of the value of trade that has passed through the NAFTA countries.

Fiction #5: *NAFTA investor-state arbitration weakens the ability of governments to regulate in the areas of health and the environment.*

Fact: *NAFTA investor-state arbitration in no way weakens the ability of governments to legitimately regulate health and the environment.*

- NAFTA investor-state arbitrations are about the application of bedrock international law obligations to specific governmental measures. When the NAFTA parties entered into the treaty they agreed to abide by long-standing international obligations of due process and fairness, and undertook to limit discrimination on the basis of nationality, subject to specific exceptions. The premise for entering into the agreement was the understanding that trade and investment liberalization enforced through a rules-based system would provide the NAFTA parties with more benefits than costs.

- Critics of NAFTA investor-state arbitration claim that the Ethyl, S.D. Myers, and the Metalclad arbitrations represent investor's use of international agreements in order to weaken environmental protections. In light of the factual record of these individual cases, such a contention simply does not accord with reality. The NAFTA arbitrations thus far have only tangentially been related to environmental issues and have been invoked ex post facto to justify blatantly protectionist government policy. In the S.D. Myers NAFTA investor-state arbitration, the tribunal made the following comments about this very issue and stated:

> ...S.D. Myers does have a valid claim. It was discriminated against by the Canadian government. The export ban that the Government of Canada imposed was not necessary. *The ban was motivated largely by a desire to promote the economic interests of the Canadian competitors of S.D. Myers.* Any legitimate concerns that Canada had over safety and environmental protection could have been readily satisfied by measures that did not exclude S.D. Myers from the market.
>
> *By pursuing a largely protectionist agenda here, Canada did miss an opportunity that was in both the economic and environmental interest of the country.* The safe and relatively low-cost option offered by S.D. Myers would have enabled Canadian owners of PCB wastes to proceed more expeditiously to get rid of them and to do so at a low cost.
>
> *There was in this case no intrinsic tension between the free trade guarantees in NAFTA and Canada's interest in protecting the environment.* Rather, taking advantage of the options offered by U.S. participants in the market, including S.D. Myers, would

actually have promoted the protection of the Canadian environment.[22]

- A fundamental weakness of the arguments from those opposing NAFTA investor-state arbitration is that they continue to propound on the "possibilities" and not the realities of what has been adjudicated. This anticipatory stress is most acute in the United States where tremendous attention has been focused on what could happen in, for example, the Loewen and Methanex NAFTA investor-state arbitrations. In the former the case was dismissed, and in the latter the tribunal has not yet rendered any decision on the merits. The fact that an investor has launched a NAFTA investor-state claim is by no means indicative of its ultimate success or failure.

- In all the NAFTA arbitrations involving Canada, the facts disclose some fundamental unfairness and high-handedness by the Canadian government towards a U.S. investor. When classic protectionist intent underlying these discriminatory actions has been uncovered by NAFTA tribunals, the Canadian government has reported back to its public that NAFTA Chapter 11 is being used by U.S. investors to weaken the ability of government to protect the environment, when clearly no such environmental protection objective was ever legitimately intended. More than anything else, these misleading declarations by governments have resulted in a profound loss of confidence in the handling of NAFTA by all NAFTA governments. This is most powerfully illustrated in the S.D. Myers arbitration.

Fiction #6: *Does investor-state arbitration limit governmental sovereignty?*

Fact: *No — by definition it cannot.*

- Critics claim that NAFTA imposes unfair limits on democratic governments and that, somehow, international rules are diminishing the sovereign ability of governments to pass laws.

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[22] *S.D. Myers*, Arbitration, Separate Opinion of Dr. Bryan Schwartz, November 12, 2000, paras. 21, 22, and 23. [Emphasis added.]

This is often referred to as the "regulatory chill" effect of NAFTA. These criticisms are unfounded.

- NAFTA imposes rules that each NAFTA government agrees to follow regarding the treatment of investors from other NAFTA countries but these behavioural limits were explicitly agreed to by those democratic governments through their elected national legislative bodies. International law is already a part of domestic law in each of the three NAFTA countries. Democratic principles require legislatures and courts to obey their international obligations once these obligations form a part of that country's domestic law. Domestic lawmaking needs to be consistent with international law in the same way that it has to follow human rights or constitutional law. NAFTA did not invent this long-standing obligation, it merely followed it. NAFTA was passed by democratically elected governments. To now suggest that NAFTA is undemocratic and interferes with governments' ability to regulate is simply not credible.

Fiction #7: *International investment agreements do not respect law or democracy.*

Fact: *These agreements are designed to guarantee and expand respect for law and democratic governance.*

- NAFTA encourages good governance and respect for the rule of law in international economic relations. The NAFTA investor-state cases thus far demonstrate situations where legal regimes in Canada and Mexico have fallen short of what is reasonably accepted as expected behaviour by market participants. Canada's federal government in at least two cases, and a Mexican local government in another have been found to have acted unfairly towards U.S. investors. In all of these cases, a fundamental unfairness has been exhibited, accompanied by some thinly veiled old-fashioned trade protectionism masqueraded as legitimate public policy. However, in the two Canadian cases, it was equally clear that the American investors would have been unable to succeed before Canadian courts because of highly discretionary Canadian laws that permit the Canadian government to suppress incriminating evidence about government decisionmaking from Canadian courts without any judicial review.[23]

- With respect to Canada, the majority of NAFTA claims have been connected to public policy failures. These failures have consisted of denials of due process, and the arbitrary and unfair treatment of foreign investors and their investments. Where these policies were the exception, rather than the rule, NAFTA ensured that fairness and due process reigned supreme.[24] It is where these public policy failures occurred that investors have succeeded.

Fiction #8: NAFTA investor-state panels act in secret and away from public scrutiny.

Fact: All NAFTA investor-state arbitration results have been made public and recent cases have been conducted in public.

- NAFTA incorporates the mechanism of international dispute settlement within its text. Under traditional international law, the techniques of mediation and arbitration are used. These alternative dispute resolution techniques rely on confidentiality in order to shorten the period of the dispute. Like all international tribunals, NAFTA uses these traditional techniques, however the disputing parties are entitled to make the proceedings public if both disputing parties agree. Public pressure on governments has in fact forced them to agree with the suggestions of investors to open the NAFTA process to the public.

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[23] One NAFTA tribunal has already looked at these rules that permit one senior Canadian official to suppress evidence and to prevent Canadian courts from engaging in any review of this order. This tribunal found the application of this procedure to be unfair to a foreign investor in a NAFTA case. However, Canada declined to follow the tribunal's request and admit the evidence or provide any specific reasons as to why some form of privilege should apply to keep the documents away from the tribunal. See Pope & Talbot, Award on Document Production.

[24] In the *Ethyl* claim, Ethyl Corporation offered to withdraw its NAFTA claim if the Canadian government would agree to an independent scientific study of its product. Furthermore, in its award on jurisdiction, the NAFTA tribunal condemned Canada's bad faith attempts to prevent any meaningful consultation between the disputing parties. In the *S.D. Myers* claim, Canada simply refused to consult with S.D. Myers about its plainly discriminatory export ban targeted against that company in the official government regulation impact statement. Myers waited a full year for consultations without any success before bringing its NAFTA claim. These failures to consult escalated into additional governance policy failures.

- For example, the NAFTA claim between United Parcel Service and Canada had its jurisdiction hearing open to the public in Washington, D.C. In this claim, the entire factual record has been made public and the tribunal established a process to consider public input. Also, the entire factual record, including evidence and transcripts of hearings has been made public in other NAFTA investor-state cases, including the S.D. Myers claim and in the Pope & Talbot claim.
- Claims about the secrecy of NAFTA investor-state panels are simply overwrought. NAFTA hearings can be as public and accessible as domestic cases.

Conclusion — Winners and Losers

The objective of the NAFTA investment chapter was to ensure that governments acted fairly and transparently when dealing with all NAFTA citizens. These objectives have been met. These tribunals have not failed to identify harsh government treatment of foreign investors. At all times these tribunals have followed the process of rules-based decisionmaking called for by NAFTA. On the whole, the decisions of the NAFTA tribunals have been restrained and highly deferential to governmental decisionmaking.

Canada set out its views ideas on what NAFTA was to accomplish in its NAFTA Statement on *Implementation*. This document states:

> For the business sector, Canadian tradecraft involves establishing a more stable and more predictable economic climate at home and abroad. It recognizes that business thrives in an orderly setting and stagnates when there is sudden and unpredictable

> change. Only by having a set of rules which treat all traders the same, which are widely known and uniformly applied and which provide for the orderly and equitable resolution of disputes will entrepreneurs have the confidence to compete, invest in the future and look beyond their own shores. And only if we can have a business sector that has confidence about its future can we expect it to invest, innovate and generate jobs with a future (Canada 1994).

Canada apparently expected the NAFTA investment chapter to create orderly rules and to have an equitable resolution of disputes. Thus it appears clear that the NAFTA investor-state process has worked as it was designed. NAFTA investors have won or lost their claims based on the merits of their cases while the objective of having stable and predictive economic rules has apparently been met.

The attempt to pass off trade protectionism under the false rubric of environmental protection does not work. The advent of greater access to information by the public now means that all citizens can and will find out about the true nature of governance. International tribunals and international publics will not be duped by inappropriate government justifications that attempt to conceal trade protectionist policies.

There have been winners and losers under NAFTA. Losers have included vested interests who have relied upon special access to advantage local business at the expense of foreigners. NAFTA has made governments accountable to independent and neutral panels to ensure respect for the rule of law and fair treatment. This is particularly valuable for small businesses that do not have access to lobbyists and other political operatives to advance their business interests. No doubt some government officials will be displeased with changes, which impose fairness limits on their absolute discretion. It is clear that these officials will continue to be unhappy with the NAFTA regime, which protects the public from their otherwise unrestricted authority. Indeed, NAFTA creates even greater pressures on domestic governments to update their own practices in this regard and create greater due process rights for all their citizens. The clear winners have been general consumers, businesses that export that have been able to achieve gains from increased competitiveness, and the general public who are best served by fair and open government. They have all received guarantees of better government processes and better value under NAFTA.

This is not to say that the process of managing NAFTA has been outstanding. The management of this large-scale economic transformation has been uneven and the level of communication between government and the public, and even between various levels of government, has been poor at times. Certainly, governments could make improvements in this regard for future investment agreements.

It has been difficult to separate the facts from the fiction about the NAFTA investment chapter. In looking at its operation, it is clear that this process has not proven to be the slayer of state sovereignty made out by its critics but part of the NAFTA process of integrating the North American economy. The NAFTA investment chapter has been a success for the public and public policy. This can be seen by new transparency in Mexico, which has been forced to make its laws public if they apply to foreign investors, and in Canada, which has had to reconsider its occasional lapses of high-handed tactics against Americans. These developments are far from negative and it is hoped that they will form the basis of further good governance as the integration of the three North American economies continues. Thus, it is safe to conclude that the NAFTA tribunals have followed in the careful footsteps of over 100 years of investor-state tribunals. They have adjudicated facts and, in appropriate circumstances, compensated investors who have been treated unfairly by foreign governments. Protecting stability and enhancing predictability through fairness and due process is exactly how NAFTA was designed to operate. Despite the proliferation of urban myths to the contrary, it is reassuring to find that this is in fact the way that the NAFTA investor-state tribunals have operated.

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In the Eye of the Beholder:
A Commentary on Investor Protection under NAFTA

Milos Barutciski

The North American Free Trade Agreement (NAFTA) negotiations provoked public controversy in all three countries that are party to the accord. The controversy was such that in 1993, shortly before the conclusion of NAFTA, President Bill Clinton made it a precondition of the United States' signing that side agreements on labour and the environment be added to the deal. In a similar vein, the newly elected Canadian government led by Prime Minister Jean Chrétien — whose party had opposed free trade while in opposition — agreed to ratify NAFTA only on condition that two trilateral working groups be established at the eleventh hour to address outstanding issues relating to the administration of antidumping and countervailing duty measures. Surprisingly perhaps, the investor protection provisions in Chapter 11 of NAFTA did not figure prominently, if at all, in the early controversy surrounding NAFTA. How things have changed.

Less than nine years after NAFTA took effect, there were only five final decisions rendered by arbitral tribunals constituted under Chapter 11, and one settlement.[1] Despite this rather meagre jurisprudential record, commentators and government officials have made wildly contradictory claims about the interpretation and potential impact of Chapter 11.

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[1] *Pope & Talbot*, *S.D. Myers*, and *Metalclad* gave rise to awards in favour of the investor; the investors' claims in *Azinian* and *Waste Management* were dismissed; and *Ethyl* was settled. For a listing of the complaints referred to here, please see Table 1 in the volume's concluding section.

Barry Appleton, in his chapter in this volume, gives a bullish endorsement to Chapter 11, seeking to debunk what he calls the "myths" surrounding investor-state dispute settlement on all fronts. Mr. Appleton says that Chapter 11 offers little if any new substantive law, and does not threaten national sovereignty or the ability of governments to regulate legitimately in the public interest (especially in the areas of health and the environment). Indeed, according to Mr. Appleton, far from being a threat to law and democracy, investment rules such as those embodied in Chapter 11 "are designed to guarantee and expand respect for law and democratic governance" (Appleton, this vol., Fiction 7).

Other commentators, such as Professor Stephen Clarkson, who also has a chapter in this volume, beg to differ. They raise an alarm regarding the questionable democratic legitimacy of unelected and unaccountable international arbitrators standing in judgment over laws and regulations promulgated by elected officials, ostensibly in the public interest. Professor Clarkson also expresses concern regarding the imposition of an extraneous "constitution" on sovereign nations through the medium of such trade and investment agreements as NAFTA, which are negotiated by unelected trade bureaucrats and international lawyers (Clarkson 2002). Yet other opponents of NAFTA — and of trade liberalization more generally — take a more strident stance and describe Chapter 11 and its bilateral equivalents as a "corporate bill of rights" designed to advance the interests of multinational corporations over the democratic will of citizens.

Throughout this controversy, the three NAFTA governments — Canada, the United States, and Mexico — sit strangely noncommittal on the sidelines and more than a little defensive, making reassuring noises about the importance of investor protection, punctuated by periodic hand-wringing over "rogue panels" and the need for greater "clarity" to reinforce their "true intent" in negotiating Chapter 11.[2] A bemused citizenry might well suspect that the impact of Chapter 11 — like beauty — lies primarily in the eye of the beholder. In fact, the matter is both more complex and more ambiguous than these and other protagonists might lead us to believe.

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[2] On July 31, 2001, the NAFTA Free Trade Commission, made up of the three trade ministers of the NAFTA countries, issued a document entitled ...

This paper addresses some of the issues that have arisen from the Chapter 11 jurisprudence. It is not a comprehensive review, focusing instead on the minimum standard of treatment (Article 1105), expropriation (Article 1110), and the more systemic issue of transparency. Of course, the jurisprudence has raised important concerns with respect to other matters, including national treatment, most-favoured-nation (MFN) treatment, performance requirements, and assessment of damages. These issues are addressed in other papers in this volume and will no doubt prompt further commentary as the jurisprudence evolves.

The Record to Date

As of April 30, 2002, 16 claims under Chapter 11 proceeded to the stage of requests for arbitration: four each against Canada[3] and the United States,[4] and eight against Mexico.[5]

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footnote 2 cont'd

... "Notes of Interpretation of Certain Chapter 11 Provisions," ostensibly as a joint interpretation pursuant to Article 1131(2) of NAFTA (the Interpretation). The Interpretation purports to address some of the concerns identified above, notably with regard to transparency of panel proceedings, the meaning of "fair and equitable treatment," and "full protection and security" in the context of the minimum standard of treatment obligations in Article 1105, and the relationship between contraventions of other NAFTA provisions (or other international obligations) and the defending government's obligation under Article 1105 (NAFTA 2001).

[3] *Ethyl, Pope & Talbot, S.D. Myers*, and *UPS*.

[4] *ADF Group, Loewen, Methanex*, and *Mondev*.

[5] *Adams; Calmark Commercial Development, Inc.; GAMI Investments, Inc.; Feldman; Metalclad; Azinian.*; and *Waste Management, Inc.* (two cases).

Overview

Not all of these claims have actually proceeded to arbitration. In addition, 14 notices of intent to submit a claim to arbitration appear to have been served on one or another of the NAFTA governments, but have either been settled or abandoned, or have not yet proceeded to the stage where a claim for arbitration has been made.[6] Six cases are complete, resulting in three awards in favour of the investor, one settlement, and two dismissals.[7] Although this is too sparse a jurisprudential record to permit firm predictions of the long-term development of the Chapter 11 jurisprudence, it is possible to discern some key themes that are emerging (Soloway 2003; Johnson 2003; and Weiler 2003).

First, when reviewing the cases where awards have been made in favour of the investor, I am struck by the arbitrary, capricious, or otherwise egregious nature of the government conduct that ultimately led to findings of liability against the country involved. In order to discipline such behaviour, the tribunals appear to have taken a relatively expansive view of the "minimum standard of treatment" obligations under Article 1105. Second, the tribunals have tended to be somewhat expansive with regard to the type of interests that might qualify as investments and are therefore subject to the protection of Chapter 11 of NAFTA. Third, the NAFTA tribunals appear to have been more cautious in their interpretation of the expropriation provisions of Article 1110 than some of the more vocal critics may have feared, and their decisions have generally been consistent with prior rulings of international tribunals that have considered expropriation of investments in the past.

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[6] As of April 30, 2002, Crompton Corp., Ketchum Investments, Inc., Signa S.A., Sun Belt and Trammell Crow Co. had filed Notices of Intent against Canada; Calmark Development Inc., Frank, Haas, Halchette Corp. and International Thunderbird Gaming Corp. had filed Notices of Intent against Mexico; and Baird, Canfor Corp. and Kenex Ltd. had filed Notices of Intent against the United States. Canfor, Frank, Kenex and Thunderbird susequently took additional steps. For a summary of all cases through late 2005, see Table at the end of this volume.

[7] *Pope & Talbot* should arguably be counted as a split decision because the investor's principal claim was dismissed by the tribunal. Nevertheless, the Canadian government appears to have snatched defeat from the jaws of victory by reason of its unreasonable conduct toward the investor during the course of the proceeding.

High-Handed and Arbitrary Conduct Begs a Remedy

Three cases have resulted in awards in favour of the investor: *Metalclad, S.D. Myers,* and *Pope & Talbot.* In each of these cases, the investor presented evidence to demonstrate that the government had engaged in highhanded, capricious, or arbitrary conduct to the detriment of the investor. In all three cases, the objectionable conduct was found sufficient to trigger liability on the basis of the minimum standard of treatment obligation in Article 1105.

In *Metalclad,* the investor had devoted considerable time and resources to construct a hazardous waste disposal facility on the strength of federal government assurances that all required approvals had been obtained. Despite these assurances, a local municipality issued a cease-work order, ostensibly on the basis that the investor had failed to obtain a municipal construction permit. Upon obtaining further assurances from the federal government that the municipality did not have jurisdiction over the facility, the investor proceeded to complete the project. At the last minute, when it was preparing to open the facility, the local municipality refused to issue the relevant construction permit on the basis of reasons found by the tribunal to be irrelevant to its proper jurisdiction. Shortly thereafter, the local state governor, who had previously supported the project, issued an "ecological decree," declaring the site a part of an ecological preserve for rare cacti and prohibiting its use as a waste disposal site. These last-minute regulatory impediments were imposed in spite of the fact that the investor had been openly engaged in the project for several years with the knowledge of the federal, state, and municipal authorities. The *Metalclad* tribunal concluded that the treatment of the investor by the state and local authorities violated the "fair and equitable treatment" requirement of Article 1105 of NAFTA.[8]

The *S.D. Myers* case arguably presented equally questionable conduct on the part of senior government officials. In that matter, the investor had been working for some years to have a United States' ban on the import of PCBs lifted so that it could use its Ohio waste incinerator to dispose of PCBs from Canada. When the U.S. import ban was finally lifted, the Canadian government imposed an emergency ban on the export of PCBs from Canada. The record was replete with evidence that the government had acted with the ulterior motive of favouring Canadian-owned competitors of the investor, rather than advancing any legitimate environmental objectives. Indeed, there was evidence of concern within Environment Canada that the ban itself would give rise to greater environmental risk. The tribunal took note of this evidence and concluded that the export ban violated the minimum standard of treatment provisions in Article 1105, as well as the national treatment provisions in Article 1102 and the performance requirement provisions of Article 1106.

Finally, in *Pope & Talbot*, the company complained that it had been injured by the Canadian government's administration of the Softwood Lumber Agreement in the allocation of export quotas to the United States. The tribunal's interim award dismissed the claims based on Articles 1102 (national treatment), 1106 (performance requirements), and 1110 (expropriation). The tribunal's final award dealt with the claim for breach of the minimum standard of treatment under Article 1105. Although the tribunal dismissed the investor's original claims to the effect that the government's allocation of export quotas under the Softwood Lumber Agreement were contrary to Article 1105, the government's conduct during — but collateral to — the litigation gave rise to an independent and ultimately successful claim that the government had violated its obligation to provide fair and equitable treatment pursuant to Article 1105. After the Chapter 11 complaint was initiated, the Softwood Lumber Division (SLD) of Canada's Department of Foreign Affairs and International Trade insisted on a "verification review" of Pope & Talbot's records in support of its export quota allocation for earlier years. Such a review would likely have been unobjectionable in itself had the SLD not insisted on conducting the review in Canada, rather than at the company's head office in Portland, Oregon, where all corporate and accounting records were located.

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[8] Mexico subsequently challenged the award in the Supreme Court of British Columbia (the seat of the arbitration). *United Mexican States v Metalclad*, 2001 — www.naftaclaims.com. Because the court interpreted the "fair and equitable treatment" provision as being equal to customary international law in which no transparency obligation exists, the court held that the tribunal went beyond the scope of the submission to arbitration, and the award relating to Article 1105 was vacated.

In this regard, it should be noted that verifications are routinely conducted in international trade matters, and particularly in customs valuation, antidumping, and countervailing duty cases where they generally take place at the venue where the company's records are located. Indeed, since a verification is essentially a form of audit, it would have made little sense to conduct such an exercise anywhere else. The SLD's insistence that the company transfer several truckloads of records to Canada was not only highly unusual to anyone familiar with the administration of international trade laws, but also counterproductive to the goal of a verification review as well as being needlessly oppressive to the company. The tribunal concluded that the investor was "being subjected to threats, denied its reasonable requests for pertinent information, required to incur unnecessary expenses and disruption in meeting SLD's requests for information, forced to expend legal fees and probably suffer a loss of reputation in government circles."[9] In particular, while it may have been within the government's discretion to require a verification review, the circumstances of the review and the manner in which it was conducted gave rise to suspicion that this was an instance of arbitrary retaliation by the SLD for the investor's decision to invoke its rights under Chapter 11. Looking at the tenor of SLD's communications with the investor and the appearance that government officials had made less than forthright reports to the minister regarding the conduct of the investor, as well as the dispute between the investor and SLD, the tribunal found that the verification episode was a denial of fair and equitable treatment, contrary to Article 1105.[10]

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[9] *Pope and Talbot*, 87.

What is particularly striking in the Article 1105 cases is the extent to which governments have defended conduct that is discriminatory, arbitrary, or capricious.[11] Indeed, international tribunals, like domestic courts, do not much care for highhanded and arbitrary conduct on the part of litigants that appear before them and are understandably inclined to find a remedy where the conduct in question offends basic principles of justice and fair play. Thus, when the Canadian government defended the conduct of its officials in the *Pope & Talbot* case by arguing that the Article 1105 cause of action was limited to "egregious" conduct (*Pope & Talbot*, 108),[12] it was arguably correct, though not for the hoped for reasons. In recognizing the evolutionary nature of customary international law, the Chapter 11 panels appear to have acknowledged that the threshold for "outrage" in the international community is lower today than it may have been in the 1920s. To the extent that the panels have raised the bar for governments with respect to the minimum standard of treatment, it is submitted that this is a positive development well in line with the tendency of domestic courts to look behind the form and to address the substance of a dispute.

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[10] It is interesting to note that, subsequent to the delivery of this conference paper, the tribunal in the *Feldman* case against Mexico issued its award finding a *de facto* violation of national treatment as a result of the application of certain tax measures. In its reasons, the majority decision of the tribunal makes pointed reference to certain conduct (denial of registration as an export trading company and initiation of an audit) engaged in by the government *after* the investor had initiated its Chapter 11 claim. One may assume that the majority of the *Feldman* tribunal, like the *Pope & Talbot* tribunal, was suspicious that these government actions were motivated at least in part by a desire to retaliate against the investor for invoking its legal rights under Chapter 11.

[11] The *Ethyl* case, which was settled before proceeding to arbitration, is a further instance of arguably egregious and discriminatory government conduct. In that case, the government passed a bill that was clearly targeted at one U.S. manufacturer. Although the bill did not prohibit the production and sale of the MMT gasoline additive manufactured by Ethyl, it had the effect of making it impossible for the investor to economically supply the Canadian market by prohibiting the import or interprovincial shipment of MMT. In effect, the investor would have had to build a plant to manufacture MMT in each province or territory where it wanted to sell the product. The bill was passed as a one-off trade measure, and subsequently defended by Canada as a health and environmental measure, despite the fact that federal health and environment officials had concluded that there was no scientific basis for banning the product under existing health and environment legislation.

[12] The government relied on the articulation of the minimum standard of treatment in the *Neer* case as conduct "that should amount to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency."

In interpreting Article 1105, tribunals have drawn from various sources of international law, including bilateral investment treaties and customary international law. This is to be expected and is indeed required by Article 1131 of NAFTA, which establishes the "Governing Law" for investor claims. Article 1131 provides as follows:

Article 1131: Governing Law

> 1. A Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law.
> 2. An interpretation by the Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section.

Article 1131 thus establishes the frame of reference for Chapter 11 tribunals by requiring them to advert to both NAFTA and "applicable rules of international law." Thus, when interpreting Chapter 11, tribunals are empowered to look beyond the four corners of NAFTA and to draw from relevant rules of international law, which include, but are not limited to, customary international law. Thus, for example, a tribunal would be entitled to consider the Vienna Convention on the Law of Treaties as an aid to interpretation, as well as other relevant international law norms, be they conventional or customary.

An important issue of interpretation in the context of the minimum standard of treatment due to investors and their investments is whether the concepts of "fair and equitable treatment" and "full protection and security" are additive or illustrative of "international law" as used in Article 1105.[13] This issue has attracted the attention of several panels with differing conclusions.[14] Panels have drawn on a wide range of sources of international law to determine this issue, as is required by Article 1131. At the same time, Article 1131 expressly authorizes the NAFTA Free Trade Commission (FTC) to issue interpretations of Chapter 11 that are binding on tribunals constituted under that chapter. The FTC issued precisely such an interpretation (the Interpretation), which made the following statements with regard to Article 1105:

> *B. Minimum Standard of Treatment in Accordance with International Law*
>
> 1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.
> 2. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens. (NAFTA 2001)

The Interpretation raises several issues. First, by purporting to limit the scope of protection to customary international law, despite the fact that the word *customary* does not appear in Article 1105, is the FTC interpreting or amending Article 1105? Second, is this issue justiciable before a Chapter 11 tribunal, or is the tribunal "bound" by an FTC interpretation regardless of whether it can be said to amend as opposed to interpret a provision? Third, even if the Interpretation is binding on a tribunal, does it have any bearing on a claimant's ability to invoke the most-favoured-nation provisions in Article 1103 by arguing that it is entitled to the better of the treatment accorded under 1105 or another bilateral investment treaty to which the respondent NAFTA government is party? These important issues remain to be decided by a Chapter 11 tribunal.[15]

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[13] Article 1105(1) provides that: "Each party shall accord to investments of investors of another party treatment in accordance with international law, including fair and equitable treatment and full protection and security."

[14] The tribunals in *Metalclad, S.D. Myers, Mondev,* and *ADF Group* each interpreted the obligation to provide fair and equitable treatment as illustrative of the minimum standard of treatment. In contrast, the tribunal in *Pope & Talbot* found that the obligation was additive to the minimum standard of treatment.

Definition of Investment

Article 1139 provides a very broad definition of investment.[16] Appearing to take their cue from this definition, some tribunals have arguably taken an even broader view as to what might constitute an investment. For example, the *Pope & Talbot* tribunal concluded that "access to the U.S. market is a property interest" and is therefore an investment "subject to protection under Article 1110."[17] The tribunal did not engage in any detailed analysis of the definition of investment in Article 1139, other than to note that it includes "property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes."[18]

The tribunal rejected Canada's argument that the ability to sell softwood lumber from British Columbia to the United States is an "abstraction" and stated that "it is, in fact, a very important part of the "business of the Investment."[19] While this is undoubtedly correct, it is still a considerable leap from this proposition to the tribunal's conclusion that the "ability" to export pursuant to a statutory export control regime is property, intangible or otherwise. While the definition of investment in Article 1139 is broad indeed, it is not without limits so as to encompass any and every right that could have a commercial value to a company.

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[15] The tribunal in *Pope & Talbot* considered the Interpretation and stated that it regarded it as an amendment rather than an interpretation. However, these comments were in *obiter*, and the tribunal did not make an actual finding to that effect. In the *Mondev* award after the delivery of this conference paper, the tribunal acknowledged the power of the FTC to make the Interpretation and viewed themselves bound by it. In *ADF Group*, another award issued subsequent to the delivery of this paper, the tribunal did not consider the issue of whether the Interpretation was an amendment or a clarification, stating that they had no authority to make such an inquiry.

[16] NAFTA Article 1139 defines investment to include equity and debt security of an enterprise; loans to an enterprise; an interest in an enterprise; real estate or other property, tangible or intangible, etc.

[17] *Pope & Talbot*, 96

[18] *Pope & Talbot*, 97.

[19] *Pope & Talbot*, 98.

There is an important distinction between property and a regulatory *right* or *licence* of the kind conferred to exporters under the Softwood Lumber Agreement (or the implementing measures adopted under the *Export and Import Permits Act*), which the tribunal appears to have glossed over. The tribunal may have stretched the definition of investment beyond the breaking point. A close reading of the tribunal's reasons suggests that it may have been induced to make this determination in a misguided attempt to shoe-horn the facts of the matter into a framework that would allow a full-blown analysis of the expropriation provisions. This is ironic because the tribunal ultimately dismissed the investor's claim for expropriation after concluding that expropriation requires a showing that the investor suffered a "substantial deprivation" of the ability to enjoy property. However, that inquiry would have been avoided entirely had the tribunal simply concluded that the "right" or "licence" to export was not itself an "investment" or a property interest. That the inquiry was unnecessary is further underscored by the fact that there was no dispute in the case that Pope & Talbot was an investor for the purposes of Chapter 11, given its extensive operations and property in Canada. That determination did not hinge on the characterization of its ability to export to the United States within the framework of the Softwood Lumber Agreement.

Had the tribunal found that Canada's administration of the Softwood Lumber Agreement resulted in a "substantial deprivation" of the investor's property in timber rights, it might have legitimately concluded that an expropriation of those property rights had occurred, as contrasted with an expropriation of the "ability" to export lumber. Ironically, the tribunal did not find any such "substantial deprivation" on the facts of the matter. Thus, in my view, the finding that "access to the U.S. market" is a property interest is superfluous and of little persuasive authority with regard to future interpretations of the scope of "investment."

In contrast to the *Pope & Talbot* tribunal's expansive definition of investment, the *S.D. Myers* decision appears to have adopted a more conservative approach. The tribunal in that case easily acknowledged that the investor's Canadian subsidiary was an "enterprise" and was therefore explicitly covered by the definition of investment in Article 1139. This conclusion seems incontrovertible, given the active operation over a period of time of the investor's Canadian subsidiary, including Canadian employees and a place of business.

Nevertheless, upon reading the tribunal's award on the merits, one is left with an uneasy sense that the investment interfered with was not just the Canadian enterprise, but also the investor's assets in the pre-existing waste disposal facility in the United States. In other words, while the Canadian subsidiary clearly suffered damages as a result of Canada's ban on the export of PCBs, a considerable measure of the damages claimed were arguably attributable to an investment in the United States rather than in Canada.

The tribunal awarded S.D. Myers damages of approximately C$6.05 million in respect of the Canadian government's breach of NAFTA, Articles 1102, 1105, and 1106.[20] The tribunal held that the investor's damages included the loss of the net income stream, which consisted of the loss of opportunity of the facility in the United States to process the PCBs. While some may argue that this decision expanded the concept of investment to include investments located outside the host country, the loss of such contracts did in fact result in lost revenue for the Canadian investment.[21]

Expropriation

The Chapter 11 remedy for expropriation of investments has been considered in all three of the awards in favour of investors, namely *Pope & Talbot*, *S.D. Myers* and *Metalclad*. The only decision to find that Article 1110 with respect to expropriation was violated is *Metalclad*. As can be seen from a discussion of these cases, the tribunals have generally adopted a more conservative approach to expropriation, although the *Metalclad* case arguably contains the germ of a more expansive definition.[22] The tribunal in *Metalclad* concluded that the state governor's prohibition on the operation of the facility amounted to a measure "tantamount to expropriation" within the meaning of Article 1110 of NAFTA. The tribunal held that the expropriation provisions of Chapter 11 protect investors against "interference with property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property" (*Metalclad*, para.103). This interpretation appears to focus on the notion of interference with the attributes of a property right as contrasted with the notion of deprivation, which predominates in other decisions.

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[20] The tribunal's damages award in *S.D. Myers* occurred subsequent to the delivery of this conference paper.

[21] The Canadian government sought judicial review of the tribunal's damages award (as well as its interim award) in the Federal Court of Canada, which was subsequently dismissed on January 13, 2004.

As noted above, the *Pope & Talbot* tribunal dismissed the investor's claim for compensation for expropriation and acknowledged that a government measure could result in expropriation without necessarily being discriminatory. This result follows from the language of Article 1110, which requires that lawful expropriation must meet all four conditions set out in that provision:

(a) it must be for a public purpose;
(b) it must be effected on a non-discriminatory basis;
(c) it must be in accordance with due process of law and the minimum standard of treatment in Article 1105; and
(d) subject to the payment of compensation.

Since these conditions are cumulative, an expropriation that is non-discriminatory but fails to meet one of the remaining three conditions is still a contravention of Article 1110. Second, as noted above, the tribunal found that expropriation requires a showing that the investor suffered a "substantial deprivation" of the ability to enjoy property. This important qualification suggests that there can be a significant interference with the ability to use or exploit property rights that nevertheless fall short of "substantial deprivation" and therefore does not give rise to a claim of expropriation. This distinction is perhaps more easily understood by considering the concept of property as a function of its various attributes. Thus, the expropriation rules under NAFTA may be viewed as focusing on the totality of the attributes that pertain to the expropriated property (for example, the right to use, consume, exclude others, or alienate) rather than on the extent of interference with any one or even several attributes. Third, the tribunal rejected the investor's claim that the phrase "tantamount to expropriation" could encompass something more than a direct taking, or a creeping expropriation by means of regulatory restrictions on the enjoyment of property amounting to a substantial deprivation.

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[22] In the *Mondev* case, the claimant failed in its expropriation claim because the acts that may have breached Article 1110 occurred and ended prior to the implementation of NAFTA. The claimant in *Feldman* lost its expropriation claim because the panel held that the conduct of the Mexican government (denying export tax rebates) was not tantamount to expropriation in part because there was no right to export, and the business remained under the control of the claimant.

The *S.D. Myers* case adopted a similar approach to that articulated in *Pope & Talbot*, including the view that "tantamount to expropriation" does not add anything to the scope of expropriation and merely connotes measures that are equivalent in effect. Moreover, the tribunal in *S.D. Myers* added the further point that expropriation, whether of the direct taking or the indirect creeping variety, "usually amounts to a lasting removal of the ability of an owner to make use of its economic rights," while contemplating that some circumstances may exist where a temporary deprivation might be serious enough to amount to expropriation (*S.D. Myers*, para. 283). As in the *Pope & Talbot* case, the focus of the *S.D. Myers* decision appears to be more on the substantial deprivation of the totality of the attributes of property rather than on interference with any one or several such attributes. Finally, the tribunal made the important point that "[t]he general body of precedent usually does not treat regulatory action as amounting to expropriation. Regulatory conduct by public authorities is unlikely to be the subject of legitimate complaint under Article 1110 of the NAFTA, although the tribunal does not rule out the possibility." (*S.D. Myers*, para. 281)

Outstanding Issues Raised by the Cases

The Chapter 11 case law raises a number of outstanding issues of both a procedural and substantive nature. In this section, I examine some of the concerns that have been raised and suggest possible approaches to dealing with these concerns.

On the process side, one of the strongest criticisms of the Chapter 11 dispute system is its alleged absence of transparency. Until the 2001 Interpretation (NAFTA 2001), the public disclosure of documents filed in the course of Chapter 11 claims was uneven, at best. In some instances, claims and briefs of argument were made available; in others they were not. Since Chapter 11 leaves many of the procedural aspects of specific claims to be decided by the tribunal pursuant to the applicable arbitration rules (which are chosen by the investor from among the three options presented by NAFTA), there has been much confusion as to the right of the public in general to obtain access to substantive information regarding such proceedings. In our view, this is inappropriate and fundamentally unsustainable.[23]

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[23] It is a historical anomaly that the investor-state dispute framework at the core of Chapter 11 is based on the model developed in bilateral investment treaties, the majority of which are between developed and developing countries. By and large, these treaties were aimed at providing remedies against developing-country governments because the overwhelming majority of the investment covered by those treaties flows from developed to developing countries. Moreover, the treaties adopt an alternative dispute settlement regime to the domestic legal system because of justified concerns as to the degree to which investors could expect disputes with the host government to be subject to the rule of law and impartial adjudication under domestic systems. The dispute resolution model adopted in bilateral investment treaties is based on commercial arbitration and therefore is essentially a private matter. Indeed, it is likely that many developing country governments preferred to maintain the private nature of investor disputes and fence off such disputes from the domestic legal regime. Chapter 11 adopts this model in its entirety, despite the fact that two of the three NAFTA parties are developed countries, and that the preponderance of claims to date have been brought against these two members, Canada and the U.S. There is good reason to question whether private commercial arbitration is an appropriate model for investor-state disputes between countries where transparency of public processes is generally expected and often required by law.

Chapter 11 may be used to challenge not only administrative actions of government officials but also specific laws openly adopted by democratically elected governments. Although Chapter 11 tribunals do not have the authority to strike down legislation found to contravene the relevant investment provisions of NAFTA, their ability to award damages against elected governments is a significant remedial tool that could constrain future government — including legislative — action. Citizens of democratic states that adhere to the rule of law can rightly expect that the decisions of their duly elected representatives (and the appointed officials who execute policy articulated by elected governments) will not be scrutinized and constrained behind closed doors at the behest of merely private interests. There is simply no legitimate policy reason why Chapter 11 panels should operate any differently from domestic courts in this regard. Unlike government-to-government disputes, where good reasons may prevail to maintain a measure of confidentiality while the dispute is in progress (for example, to allow governments to engage the merits of a dispute without being unduly constrained by transient political considerations that might be generated by premature publicity), investor-state disputes are essentially contests between a private interest and a public body that, ordinarily, would be conducted in the full light of day in the domestic judicial forums of each of the NAFTA parties. To the extent that proprietary or confidential business information is disclosed during a proceeding, rules have been developed in domestic courts and administrative tribunals to maintain the confidentiality of such information without jeopardizing the public nature of proceedings.

The 2001 Interpretation goes part way to remedying this problem by clarifying the right of the NAFTA parties to make public all documents submitted or issued by a Chapter 11 tribunal (subject to certain exceptions) "in a timely manner." In my view, the Interpretation does not go far enough. The phrase "in a timely manner" leaves much room for delay in publication of tribunal documents. Moreover, the right of NAFTA parties to make documents public is still constrained by the agreement's own terms for compliance with confidentiality that might be imposed under the applicable arbitral rules. Furthermore, there does not appear to be any legitimate reason why the public or non-public nature of Chapter 11 proceedings should be any different than any other disputes between governments and private claimants. The general rule under the domestic legal systems of the three NAFTA parties is that such disputes are public and the same rule arguably should apply to investor disputes under NAFTA.

A further concern arises with respect to the absence of effective review of panel decisions that are perceived as wrongly decided. This issue, like transparency, is closely tied to the notion of accountability. Some view the Chapter 11 process as lacking in accountability because it takes place behind closed doors before ad hoc panels composed of international lawyers drawn from an obscure and elite profession with little contact with the citizens of the NAFTA countries. While this criticism is arguably unfair, the fact that the ad hoc NAFTA panels are able to rule on important matters of public policy without being subject to effective review does resonate negatively with citizens in open and democratic societies.

In the absence of an institutionalized appeal or review mechanism under Chapter 11 itself, judicial review of arbitral awards in a domestic court is the only method whereby tribunal decisions can be reviewed. To date, such judicial review proceedings have been initiated and concluded in two cases, *Metalclad* and *S.D. Myers*, and in both cases at the instance of the losing governments.[24] However, it is questionable whether domestic judicial review is an appropriate vehicle for correcting problematic precedents.

First, domestic courts are poorly suited to and have no expertise in interpreting international treaties or international law more generally. Second, the limited scope for judicial review available in jurisdictions that are subject to the New York Convention (including all three NAFTA parties) makes it difficult to correct true errors of law. Third, to the extent that the courts of the three NAFTA countries adopt different approaches to judicial review of arbitral awards, there is a risk of differing interpretations and outcomes in similar cases depending on where the seat of the arbitration is located. Fourth, there is an inherent artificiality to situations such as the judicial review of the *Metalclad* decision's taking place before a Canadian court applying Canadian domestic law, despite Canada's having had no point of contact with either the investor or the responding government, or the underlying factual and legal issues.

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[24] The Canadian government challenged the partial award in *S.D. Myers*, filing a Notice of Application in February 2001, and subsequently the judicial review was dismissed. Mexico challenged the award in *Metalclad* in the Supreme Court of British Columbia (the seat of the arbitration). While the court upheld the award for expropriation, the award for damages under Article 1105 was vacated as the fair and equitable treatment provision and was not considered to include a transparency obligation.

One possible alternative may be to establish a quasi-permanent Chapter 11 appellate body modelled on the lines of the World Trade Organization's (WTO) Appellate Body. This would allow a more consistent body of jurisprudence to develop while at the same time potentially allaying fears of rogue panels. If this approach were to be followed, an important issue would be to determine the appropriate standard of review. Given the stakes involved, it is arguable that a correctness standard would be appropriate on matters of law, while great deference would likely be appropriate with respect to findings of fact in order to preserve some of the benefits of the commercial arbitration model.

Another option may be to seek the establishment of a multilateral appellate body for matters of investment law, perhaps under the auspices of the International Centre for the Settlement of Investment Disputes (ICSID).[25] Given the more than 2,300 bilateral investment treaties in existence today, there may be significant merit in establishing such a multilateral institution with a view to promoting a consistent evolution of international investment law. A variant of this may be to co-opt the WTO Appellate Body itself. Given the close linkages between the rights conferred by investment treaties (national treatment, MFN) and WTO rules, as well as the gradual development of investment rules under the WTO (for example, the Agreement on Trade-Related Investment Measures and the General Agreement on Trade in Services), there would be merit in promoting greater convergence between different but related fields of international economic law.[26]

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[25] The centre was established pursuant to the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention). The centre's extensive experience with investment disputes, together with the fact that 154 countries have signed the convention make it a potentially useful forum for the establishment of a permanent appellate tribunal for investment matters. Unfortunately, its potential application in NAFTA Chapter 11 disputes is uncertain because Canada and Mexico are among the few significant importers of foreign investment that have not yet signed the ICSID Convention.

Another aspect of Chapter 11 that is often considered as a candidate for further clarification is the relationship between the expropriation rules and government power to regulate without being potentially liable for expropriation (also referred to as *police power*). Indeed, it is not entirely clear from the existing jurisprudence whether such a sphere of immune regulation exists under international law. As a result of this outstanding ambiguity, it has been suggested that the current rules on expropriation, and specifically the concept of *tantamount to expropriation*, have had a chilling effect on the ability of governments to regulate in the public interest as well as on their willingness to do so for fear of provoking a Chapter 11 claim.

For the reasons already outlined, I suggest that much of the hand-wringing about this issue to date is not warranted by the jurisprudence, which is on the whole quite conservative. Nevertheless, the perception is real and the continuing uncertainty surrounding this issue threaten to greatly undermine public and international support for maintaining robust rules against expropriation.

Efforts to articulate a definition of the police power often run aground on the shoals of determining its proper scope. The most difficult task appears to be to articulate rules that do not suffer from under-inclusion, such as leaving governments potentially liable to pay compensation for regulation, or prohibition of activities that are inherently injurious to life, health, public safety, or some other peremptory public interest,[27] or over-inclusion, such as allowing governments to regulate in a manner that amounts to de facto expropriation without compensation in the absence of a rationally defensible and overriding justification.[28] We suggest that a comprehensive delimitation of the police power is not necessary to significantly reduce the perceived risk of regulatory chill arising from an unqualified obligation to compensate for regulatory activity that may reach the threshold of being tantamount to expropriation. Thus, there may be some merit to a limited interpretation by way of an Article 1131 to confirm the existence of a police power to regulate in the public interest; that it is limited to the protection of life, health and public safety, in contrast to, for example, economic, social, or cultural regulation, and that bona fide exercise of the police power does not attract liability for expropriation. The precise scope of the police power, on the other hand, would be left to future panels to determine on a case-by-case basis.[29]

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[26] An ad hoc arrangement under which the WTO's Appellate Body might sit on appeals from investor-state tribunals might, however, be difficult to achieve in view of the great resistance of many developing country members of the WTO to see that organization's mandate expand into the investment sphere.

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[27] For example, suppose that a pharmaceutical company makes a massive investment in developing a particular drug that has important therapeutic qualities. The drug is tested and ultimately approved for human use. The company makes further investments in a plant to manufacture the drug as well as in its promotion and distribution. If, some years later, the drug is discovered to have unforeseen and highly dangerous side effects that cannot be effectively remedied by restrictions on its use, the government should be entitled to prohibit its sale, without having to compensate the manufacturer for the loss of its investment in R&D, manufacturing, and distribution of the drug. In effect, the overriding public interest in protecting citizens' lives and health clearly justifies the government's actions. The investor assumes the risk that its investment may ultimately result in generating little if any value.

[28] One of the difficulties in articulating the limits of the police power arises from the fact that Article 1110 expressly contemplates compensation for expropriation that is "for a public purpose." Thus, not all categories of regulation would be immune from compensation merely on the basis that they serve a public purpose. The concept of a police power, on the other hand, opens the door to identifying a field of regulation that is immune. In other words, arguably, some public interests are so important that governments should be free to act in their furtherance without the constraint of an obligation to compensate.

[29] Such an approach, while not comprehensive, would still be highly beneficial because it would put to rest ongoing dispute as to whether there is any ...

Conclusion

As I indicated at the outset, the potential impact of Chapter 11 of NAFTA is both greater and less than many of its proponents and critics, respectively, would lead us to believe. A review of the limited jurisprudence to date shows many of the fears unfounded that companies could use Chapter 11 to bludgeon governments into paying massive compensation for implementing programs and legislation in the public interest. At the same time, Chapter 11 does create new rights and it does provide significant remedies for conduct that would have not been actionable in its absence. It is particularly notable that the Chapter 11 right that has been used to greatest effect to date is the minimum standard of treatment under Article 1105, which has been successfully invoked on several occasions to remedy government conduct that was clearly arbitrary or capricious. That such conduct is constrained by Chapter 11 is most assuredly a positive development.

On the other hand some areas of potential concern have been identified that arguably merit a response. Chief among them is the issue of transparency. Since the Chapter 11 process can be invoked to challenge virtually any government policy or measure, citizens have a right to expect that the process meets the standards of openness and accountability that they expect of other important government institutions. No amount of fine-tuning of the procedural or substantive rules will deflect the suspicion that the system is unaccountable, antidemocratic, or worse if its operation cannot be subject to public scrutiny.

As well, the debate between the right of governments to regulate in the public interest and their potential exposure to liability on the ground of expropriation is one that clearly deserves greater clarification. The current uncertain status of the matter is responsible for much of the controversy surrounding Chapter 11 of NAFTA and is impeding the legitimate objectives of promoting effective investor protection in other bilateral and multilateral contexts.

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footnote 29 cont'd

... such thing as the police power constituting a sphere of immune regulation, and focus the jurisprudential debate on the proper scope of such a power.

While a comprehensive resolution of the issue is beyond our grasp at the present time, given the disparate interests involved and the existing body of established investment treaties, there may be more limited reforms that can mitigate the most worrisome concerns that have been identified as potentially resulting from the current expropriation remedy in Chapter 11. Given the potential benefits of limited reform, this is one instance where seeking the best result should not be allowed to interfere with the attainment of a better one.

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Hijacking the Canadian Constitution:
NAFTA's Investor-State Dispute Arbitration

Stephen Clarkson

To understand the significance of the investment disciplines of Chapter 11 of the 1994 North American Free Trade Agreement (NAFTA) requires locating this economic agreement within its international context. Once having established its genealogy, we can then consider its controversial process for investor-state arbitration.

Historical Context

Prior to the advent of the Canada-United States Free Trade Agreement (FTA) of 1989, Canada's international trade obligations were set out in the 1947 General Agreement on Tariffs and Trade (GATT). Initially, an international trade organization (ITO) had been negotiated as a strong trade-policy complement to the World Bank and the International Monetary Fund (IMF) that had been set up in 1944. When the ITO fell victim to Congress's unwillingness to have U.S. policy fettered, GATT emerged as a weak arrangement limited to moderating government policy affecting international trade in goods. Compliance with its provisions was a matter of good will among its signing parties.

Fast forwarding to the mid-1980s, the United States tabled an agenda for dramatically expanding the GATT framework to include areas of economic and social regulation that had not previously been the subject of international trade disciplines and which often had little, if anything, to do with international trade in a conventional sense. Washington's motivations for demanding a transformation of the world's economic rules were complex and multifaceted: enormous and growing trade deficits; the need to secure access to strategic resources, such as oil and gas; and the global ambitions of its domestic sectors that had established a competitive lead in knowledge-driven technologies, including pharmaceuticals, software, biotechnology, and entertainment.

To accomplish its strategy to change the global regulatory system, the United States adopted a three-pronged strategy — unilateral, multilateral, and bilateral — to contain what it regarded as the excessively interventionist policies of foreign governments by requiring them to abandon export controls on energy and other strategic goods, while opening in areas where U.S. transnational corporations (TNCs) had developed global superiority.

Unilateral Measures. Washington strengthened its already powerful unilateral measures, in the form of antidumping and countervailing duty laws that it invoked either for its own protectionist purposes or to pressure other countries to abandon policies that it regarded as too restrictive to American exporters, investors, or service providers (Ostry 1999).

Multilateral Measures. At the international level, Washington wanted GATT to cover:

- Foreign investment, to improve conditions for its TNCs' overseas' operations;
- Services, to open space for its TNCs in countries that had not established competitive or open markets in such areas as telecommunications, health care, education, insurance, electricity, or cultural industries; and
- Intellectual property protection, to globalize the patent and copyright protections granted under U.S. law.

The prospects for getting members to change GATT's rules were not promising because of resistance from both North and South. The European Union (EU) wanted to maintain the state aids to industry and subsidies for its farmers that the U.S. was targeting. Leading Third-World countries, such as Brazil and India, also feared that U.S.-made economic rules would prevent them from using the same kind of supportive policies to support their entrepreneurs in the twenty-first century that the United States had used so successfully in the nineteenth.

Bilateral Measures. As a result of the political logjam at the GATT, the United States decided to pursue bilateral negotiations with more compliant trading partners with whom it hoped to set precedents that would provide prototypes for its multilateral negotiating agenda. Thus, in 1986 as it tabled proposals to expand the GATT framework, Washington was also engaged in bilateral negotiations with Canada that would culminate, a scant two years later, in the FTA's signing.

The FTA represented a radical departure from conventional notions of where the demarcation line between domestic and international trade policy naturally belonged. For the first time, a trade agreement brought the vast, but uncharted, territory of business and government services under international disciplines, which, to that point, had applied only to goods. Thus, the obligation to provide national, or non-discriminatory treatment was now to apply not just to goods or products, but to such services as banking operations and insurance contracts, legal and architectural work, health care and even education.

Another of the FTA's novel features was the incorporation of rules concerning foreign direct investment within the framework of an international trade agreement. Pursuant to these disciplines, Ottawa agreed to apply the principle of national treatment to investment. This meant that Canadian governments were now committed to treating U.S. investors the same way they treated domestic citizens and corporations — a concession that Canada had long resisted because of its economy's high proportion of foreign direct investment. By offering U.S. companies the same incentives that it might give domestic firms, Canada abandoned the kinds of industrial strategies aimed at promoting local enterprise, employment, and innovation that had formerly constituted much of federal and provincial economic policy.

The Canadian government went further with NAFTA, agreeing in Article 1106 to give up imposing "performance measures," whether or not these involved foreign investors. The constraint covered not just the federal, but also provincial and municipal governments. British Columbia, for instance, has long attached conditions to resource extraction or forest harvesting licences to increase domestic value-added processing. Municipalities often attach local purchase requirements to the contracts and approvals they give. Even if non-discriminatory, as far as the nationality of the company is concerned, such performance requirements are now forbidden.

Finally, the FTA established rules for energy trade which ensured U.S. consumers unfettered access to Canadian energy resources for as long as the agreement remained in place and at prices no higher than those charged to Canadian consumers. As a result, Canada was prohibited from imposing export controls on oil, gas, and electricity except in times of shortage. Even then, exports could not be restricted any more than domestic supplies were rationed to Canadian markets.

The second phase of North America's evolution as a trade bloc represented a simultaneous broadening and deepening of the system already established by the FTA. In January 1994, the North American Free Trade Agreement broadened the free-trade regime to include Mexico, and also expanded the FTA's limits on its signatory governments by expanding its institutional structure, adding a chapter creating extensive intellectual property rights, changing the FTA's dispute settlement mechanism, extending the coverage of its investment provisions, and adding to those investment disciplines a new dispute resolution procedure that empowered Canadian-, U.S.-, and Mexican-based corporations to sue the governments of other NAFTA parties.

One critical consequence of radically expanding the scope of international trade law in this manner, was to extend the threat of international economic sanctions to a host of domestic policies concerning services and investment, which previously had been entirely matters of national or local concern. Under these regimes, a municipal zoning ordinance may become the subject of an international claim, as may groundwater protection legislation, cultural programs to support library services, and even the pension plans of postal workers.[1]

The significance of these changes went well beyond simply changing economic policies. NAFTA's formal stipulations created at the continental level of North America a new legal order by which its three member states are bound. In fact, NAFTA established new and comprehensive disciplines to which the policies, laws, and constitutional norms of its member states were obliged to conform.

The New Trade Agreements As External Constitution

When a country signs a treaty it *internationalizes* the state's legal order to the extent that domestic laws are harmonized with the norms embodied in the accord. Before the advent of the new global trade order, literally hundreds of international treaties, conventions, and other instruments had little effect on the constitutional norms of the nation state, where legal sovereignty was barely compromised by such undertakings (Jackson 1997, 32). Weak enforcement mechanisms allowed a state to ignore or abrogate its international commitments. Nor was a government bound to comply with an international body's ruling that it considered adverse to its interests or incompatible with its culture. Even as determinedly a team player as Canada was, on occasion, willing to flout international law that challenged a constitutional norm.[2]

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[1] All of these examples are taken from investor-state claims initiated pursuant to Chapter 11 procedures. See *UPS*, *Metalclad*, and *Methanex*, which are summarized in Mann (2001). See also, at the end of this volume, a listing of the complaints referred to in this publication, "Complaints under NAFTA Chapter 11."

[2] The censure by a UN committee of the Ontario government for not extending to all religious schools the state funding that it gives Catholic public schools, challenged a key element of the 1867 confederal bargain that guaranteed Roman Catholics in the province the preservation of their educational system — and was ignored.

The literature on the political significance of NAFTA generally discusses how, in sharp contrast with most international agreements, it created a mode of economic regulation with such broad scope and such unusual judicial authority that it transformed the political order of the three states that are parties to it.[3] Taking this argument one step further, I maintain that NAFTA so closely conforms to the conventional notions of what comprises a constitution that it can best be understood as creating parts of an external constitution for its signatories.

As rule books that determine how political systems operate, constitutions generally contain five basic components.

1. *Norms*. Understood as regularized constraints on behaviour, supra-legislative norms are contained in constitutions to put certain values beyond the reach of legislators and officials.
2. *Institutions*. Constitutions define the parameters of formal rulemaking institutions, their administrative agencies, and enforcement or compliance regimes.
3. *Limits*. Constitutions also set limits to the powers of the institutions that they create.
4. *Rights*. The corollary of these limits is the rights with which the system's citizenry are endowed.
5. *Adjudication*. To interpret the ambiguities inherent in these norms, limits, and rights and to resolve eventual disputes a judicial system is required.

The rest of this section applies this model to show how NAFTA effectively functions as a constitutional instrument.

Norms. Constitutions typically entrench certain inviolate principles or norms that are above the capacity of any politician to alter, and NAFTA has done this by establishing several government-inhibiting principles that apply to all policies, regulations, and actions of member states. In agreeing that the FTA should enshrine the principle of national treatment, or most-favoured-nation treatment (MFN), Canada was not simply reiterating a commitment that it had made for goods in GATT, but was agreeing to apply these normative trade rules to investments and services as well.

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[3] The same assessment applies to the World Trade Organization and the international agreements that are organized under its administration. Indeed, the WTO's state-to-state enforcement mechanisms are significantly stronger than their corollary in NAFTA.

Thus, certain key international trade disciplines entrench supra-constitutional norms because they are established as a superior legal order, binding broad spheres of government policy, law and action. These may not be reflected in the domestic laws of the nation state, but can be enforced by international sanctions regardless of their status under, or consistency with, domestic laws or constitutional norms.

Institutions. In contrast to free trade in the European Union, NAFTA did not create continent-wide executive, legislative, or bureaucratic institutions of any substance. NAFTA's central institution, the Free Trade Commission — which consists of the three countries' trade ministers who formally retain final authority to supervise NAFTA's institutional mechanisms, resolve disputes over interpreting its text, and take whatever steps might be necessary for its future development — in practice has no permanent location or budget and amounts to little more than periodic meetings of the three ministers. NAFTA's decisionmaking was to be by consensus, which meant that each party retained a veto over common business.

Two collateral institutions were established as adjuncts to NAFTA. One, the North American Commission for Labour Cooperation (NACLC), is overseen by an executive comprised of the three national governments' labour ministers (Fernández de Castro and Ibarghen 1999, 515–32). The other, the North American Commission on Environmental Cooperation, is similarly constituted under the direction of the parties' respective federal environmental officials. The mandate of these regimes is to ensure the effective enforcement of domestic labour and environmental laws. Neither requires environmental or labour legislation to be raised to any specific threshold. Nor do the agreements prevent the signatory states from lowering environmental protections and labour rights. Having no meaningful enforcement regime, both commissions are condemned to being largely hortatory.

Limits. NAFTA contains two types of supra-constitutional limits on member states' domestic institutions, including governments at all levels, administrative agencies and tribunals, and state enterprises. Positive, thou-shalt provisions prescribe how members must rewrite, for example, their laws on intellectual property. Negative, thou-shalt-not clauses proscribe a wide range of practices, such as regulations or performance requirements of foreign direct investment.

One manifestation of NAFTA's supra-constitutional effect can be found in the specific amendments made to domestic policies, laws, and regulations in order to bring them formally into compliance with NAFTA disciplines. Normally, changes in laws and regulations are made by governments within the institutional and legal framework established by their internal constitutions and in response to demands from below by the electorate or specific functional constituencies. Unlike these normal amendments to statutes made by sovereign legislatures, which can further amend or revoke their acts in response to changing domestic considerations, statutory amendments incorporating international trade norms can be validly amended only if the external regime changes its rules by international agreement. Otherwise, democratically legitimate government actions deemed by the appropriate arbitration procedures to violate the international agreement in question will subject that government to sanctions or penalties.

Whether domestic law and policy is formally amended or not, governments must still comply with the trade rules on pain of exposing themselves to international sanctions for non-compliance. That Canada's NAFTA obligations are binding on it, whether or not it has chosen to ensure conformity of its domestic law, underlines their supra-constitutional character.

The coercive force of Canada's commitments under NAFTA and other international trade agreements can be found in the nature of the penalties that it may suffer should it fail to comply with them. It is not uncommon, for example, for international trade sanctions to be claimed in the billions of dollars with ruinously disruptive implications for the domestic economy, particularly one as dependent upon foreign trade as is Canada.

Moreover, cross retaliation allows sanctions to be targeted strategically where they will have greatest effect. For example, when the United States objected to Canada's response to an adverse WTO ruling concerning certain cultural policies protecting Canada's magazine publishing industry, it proposed to target $1 billion of Canadian exports to the United States. Steel exports from Canada, many of which were produced — not coincidentally — in the riding of Canada's then-Heritage Minister, were to bear the brunt of these threatened sanctions ("A Pitch..." 1999).

Some observers might maintain that Canada's sovereignty remains intact because it is free to abrogate NAFTA upon giving its two partners six months' notice. However, this formal right needs to be set against the political-economic dynamic in North America. Once a government has adjusted its statutes and once its economy has been restructured in accordance with the free-trade model, it becomes, practically speaking, impossible to abrogate the agreement that brought about this transformation. It is very difficult to imagine Canada's abrogating NAFTA in the face of opposition from south of the border. And the United States would certainly attempt to hold Canadian governments to the trade rules that secure its strategic objectives, not the least of which is guaranteed access to Canadian petroleum and other energy resources. The potential impact of a breakdown in trade relationships with the United States would devastate the Canadian economy, which is so dependent upon international trade, fully 87 percent of which is with the United States. So even if Canada has a *de jure* right to extricate itself from the obligations assumed under NAFTA, there is no practical possibility of doing so.

Rights. As the corollary to limiting government, a state constitution establishes specific rights for its citizens, whether individual or collective. But, in Canada, the only rights extended by continental governance are for corporations and for foreign investors and their investments. These entities and individuals not only have rights and entitlements under NAFTA not available to Canadian citizens (corporate or otherwise) but have also been accorded a unilateral right to enforce those rights against the parties to NAFTA (investor-state claims).

In 1980, when Parliament debated what should be included in the proposed new Charter of Rights and Freedoms, property rights were excluded on the grounds that they were adequately protected under the common law. In other words, the right to property was not to be absolute in Canada, but conditioned by broader societal objectives. For instance, the public interest in sound land-use planning in a municipality could have priority over the interests of entrepreneurs and developers striving to maximize the value of their property interests. But under NAFTA, private property protection is absolute. This means that an American investor could now win damages against a Canadian city on the basis that — whatever its public policy goals — the value of its subsidiary's property had been expropriated.[4]

NAFTA's Article 1110 established an absolute right to compensation, at fair market value, whenever a government measure is determined to have "directly or indirectly" expropriated a foreign investment or is "tantamount to nationalization or expropriation." Unless justified as being in the public interest, the taking of private property by governments is unlawful, quite apart from the issue of compensation. The protection of private property enshrined in these provisions concerning expropriation established another norm that is superimposed on statutory, common law, and constitutional principles concerning property.

Judiciary. Norms, limits on institutions, and citizens' rights rapidly become dead letters without a judicial system to interpret and apply the constitution's texts and authorize meaningful sanctions in cases of non-compliance. Without access to adjudication, the expansion of international trade regimes would probably not have been of any more consequence than the International Labour Organization's many conventions, which are rhetorically powerful but practically powerless. The new generation of international economic agreements, of which NAFTA is a prototype, constrains sovereign authority much more substantially than did their predecessors because of their expanded breadth and also because of their judicial mechanisms' considerable strength.

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[4] Of course, Canadian firms operating in the United States and Mexico would benefit from this right to attack American or Mexican regulations that they allege have expropriated their property.

Trade liberalization is typically promoted as a means for depoliticizing disputes that erupt periodically between nation states. Recent trade agreements address this challenge by establishing binding international rules to be immune from the political manipulation that so often characterized the application of U.S. domestic trade remedies. With the exception of Chapter 11's investor-state claims, NAFTA has not created a continental level of judicial governance. Under Chapter 19, for example, a party may seek review of another's antidumping determinations, though only for the purpose of ascertaining whether such measures are consistent with the domestic law of the party imposing the measures. The effectiveness of Chapter 20 procedures for resolving state-to-state disputes is limited, because panels only make advisory rulings, which ultimately return to the political arena for solutions to be negotiated by NAFTA's Free Trade Commission.[5] Although weak in its capacity for constraining governments' trade-remedy protectionism and for adjudicating intergovernmental trade disputes, NAFTA has established with Chapter 11 an unprecedentedly powerful mechanism through which foreign corporations may discipline governments' regulation and policymaking activities, particularly in the area of environmental controls.

NAFTA's Investor-State Dispute Arbitration

Before NAFTA, a Mexican or U.S. company whose Canadian subsidiary was hurt because of a Canadian government's action had either to defend itself within Canada's legal system or to persuade its own government to launch a trade complaint. Even if there were grounds for doing so, political leadership might have second thoughts about attacking another country's policies in this way in case it jeopardized other mutual interests, such as military collaboration. NAFTA's innovation was to put the arbitration machinery of international commercial regimes at the direct service of foreign investors who could now enforce rights they enjoyed because of an international treaty to which they were not parties, and under which they had no obligations (Levin and Erickson Martin 1996, 90).

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[5] For example, it took Mexico from 1995 to 2001 to have a Chapter 20 process rule that the United States should honour its NAFTA obligation to allow Mexican truckers to ply their trade in the American market — a ruling that was stalled by challenges in American courts.

Article 1110 provides that no government may "directly or indirectly expropriate or nationalize," or take "a measure tantamount to expropriation or nationalization" except for a "public purpose," on a "non-discriminatory basis," in accordance with "due process of law and minimum standards of treatment," and on "payment of compensation"(NAFTA, Art. 1110). This provision has now been invoked to challenge a diverse array of policy and regulatory actions taken by federal, provincial, or municipal governments that have been charged with expropriating foreign investments. This Chapter 11 prohibition of actions "tantamount to expropriation" was itself tantamount to a new constitutional property right, but one that was only available to NAFTA party subsidiaries of foreign-based TNCs (Schneiderman 1996). This has proven the most controversial of the external constitution's provisions, because it allows foreign corporations to invoke secretive international dispute procedures to challenge a broad spectrum of domestic policy and legal matters, from the delivery of postal services to the regulation of gasoline fuel additives.

Chapter 11's investor-state dispute process introduces an extraordinary foreign element into the sphere of Canadian public law. In effect, this dispute mechanism withdraws an aspect of public law from governmental control by internationalizing — though in a private tribunal format — the domestic legal process, which previously dealt with conflicts over public policy. Not only has Chapter 11 added to the Canadian constitution a new corporate property right that treats corporations unequally depending on their nationality, it has also imported an existing arbitration mechanism designed to handle international commercial disputes, turning it into a device to constrain governments' public policymaking capacity.

Arbitral rulings made under this system may be enforced directly by foreign investors (under Part B of the chapter). They are also amenable to state-to-state enforcement under Chapter 20, in which case they would ultimately depend upon the willingness of the parties to implement an adverse dispute ruling.

Because the investor-state dispute process is independent of political control, litigation pursued under its aegis exerts an influence over a broad sphere of domestic policy and law. This constraint of sovereign legislative action has several facets.

Arbitral Awards Are Binding and Enforceable

Unlike state-to-state procedures, investor-state tribunals are empowered to make damage awards, which are binding and enforceable in Canadian courts, as they are in more than a hundred nations that have agreed to the recognition and enforcement of international arbitral awards.

Unpredictability in Investor-State Litigation Creates Regulatory Chill

Because of the tribunals' independence of the political process and because NAFTA has no formal judicial structure to impart coherence, the interpretation of NAFTA's rules under Chapter 11 varies considerably from case to case. Moreover, the absence of any doctrine of judicial precedent leaves each tribunal to decide its own approach to interpreting NAFTA disciplines (Johnson 2001; Thomas 2002). This ad hoc approach, combined with the broad, sometimes novel, though often ill-defined character of many NAFTA norms, contributes to a new condition of regulatory uncertainty. Policy- and law makers wishing to steer clear of NAFTA prohibitions have to navigate a course through a minefield where the hazards are constantly shifting. As Muthucumaraswamy Sornarajah writes,

> The notoriety, cost and potential liability associated with trade challenges and investor-State claims have been described as producing a "chill" over the development of domestic policy and law by governments. Moreover the inclination to engage in this form of self-censorship is accentuated when the ambit of the constraints imposed by a particular international commitment are unknown or uncertain. Negotiators of NAFTA and officers implementing its provisions have stated that the nature of the litigation that has resulted from Chapter 11 was unforeseen. (Sornarajah 2000, 70)

There is considerable evidence that the threat of Chapter 11 litigation is sufficient to warn governments away from taking policy and regulatory initiatives that respond to democratic demands even if they are entirely legitimate under Canadian law. An illustrative case is Ottawa's debacle over cigarette packaging. In the mid-1990s, the federal government tabled proposals to ban differentiated cigarette packaging, a natural extension of its prohibition of cigarette advertising. Although the tobacco industry claimed that its packaging served no other purpose than to promote competition for existing smokers, the government maintained that branding was targeted at lifestyle marketing and thus promoted increased sales and smoking (Goodeve 1996). After being threatened with a Chapter 11 claim that the proposed legislation was tantamount to expropriation, government officials abandoned their plans.

In at least two of the actual cases brought against Canada, Ottawa has quickly settled with the disputing investor.[6] In one, Ethyl Corp. of Virginia, producer of an octane-enhancing chemical, objected to the Canadian government's banning the cross-border trade of additive MMT. Ethyl had been unable to persuade Washington to request a dispute panel against Canada under Chapter

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[6] See *Trammell Crow Company v Canada*, which can be found at www.naftalaw.org. www.dfait_maeci.gc.ca/tna_nac/gov_en.asp.

20, NAFTA's regular process for resolving conflict between governments. Since the U.S. Environmental Protection Agency (EPA) had banned MMT as a dangerous neurotoxin since 1977, Washington was unwilling to expend political capital on contesting Canada's right to ban trade in the same substance. Using Chapter 11's provision on investor-state disputes, Ethyl was able to bypass its government's reluctance to fight on its behalf. It put forward a claim that Ottawa's legislated ban on the fuel additive had cost it US$250 million in lost business and future profits (May 1998).

Canada actually rescinded its regulations effectively banning the use of the toxic fuel additive, offering Ethyl Corp. what amounted to a public apology for having regulated the substance in the first place.[7] In addition to the US$19 million paid to Ethyl as part of the settlement, and the costs of unsuccessfully defending the measure, the political embarrassment of having to beat a hasty and public retreat also exerted a constraint on government enthusiasm for pursuing future environmental and public health initiatives that might irritate foreign investors.

The MMT case revealed how Canadian environmental policy, once thought to be the purview of the sovereign legislature, has been taken hostage by continental governance. Under the supraconstitutional aegis of Chapter 11, the issue is no longer the classic Canadian question of which level of government — federal or provincial — can initiate an environmental regulation. The issue now became whether any level of government could initiate such legislation if it jeopardizes the interests of a Mexican or U.S. company (Schneiderman 1996, 535). Far from polluters' paying to rectify the externalities that they cause, Chapter 11's expropriation clause leads to the polluters' being paid to keep on polluting.

The constraining influence of these international trade agreements has already been institutionalized in domestic policy formation. The federal government has established a process for vetting policy proposals for their potential to generate damaging suits mounted by foreign governments or corporations.

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[7] While the evidence of harm associated with the use of the particular substance MMT is equivocal, most other member nations of the OECD, relying upon the precautionary principle, have banned the use of this fuel additive.

Adding to the chilling effect of these international disciplines, the range of government measures that may be subject to foreign investor claims extends beyond that for which legal sanctions would be available under the common law. Even a minister's speaking to a piece of legislation or regulation in a debate in the House of Commons about the need for an environmental regulation could attract litigation by the manufacturer of the impugned substance on the grounds that the public criticism of its product is a measure that has damaged its good will and so is tantamount to expropriation.

The Internationalization of Legal Norms. Since U.S. corporate law dominates international commercial law cases, conflicts between U.S. companies and the Canadian state will inexorably cause U.S. definitions to infiltrate Canadian legal standards and force Canadian governments to operate as if U.S. law on regulatory takings applied to them. While some observers expected that Canadian, American, and Mexican jurisprudence would interpret expropriation differently in each country (Dearden 1995, 127), it is generally acknowledged that panel findings will impose the U.S. interpretation instead of the other two signatories' legal notions.[8]

Chapter 11 dispute settlement also violates many values held dear in the common law tradition.

Judicial Sovereignty. Through the privatization of legal disputes concerning state actions, judicial sovereignty has become another casualty of this extraordinary addition to the Canadian legal order. When the location of arbitration is not in the jurisdiction where the measure is being challenged, no judicial supervision may be exercised by the challenging country's courts.

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[8] "The term *expropriation* includes, but is not limited to, any abrogation, repudiation, or impairment by a foreign government of its own contract with an investor with respect to a project, where such abrogation, repudiation, or impairment is not caused by the investor's own fault or misconduct, but materially and adversely affects the continued operation of the project" (*United States Foreign Assistance Act* of 1969, section 238, cited in Levin and Marin (1996, 97). See also Schneiderman (1996).)

Indeed, judicial review for Chapter 11 tribunal rulings can only deal with matters of jurisdiction, not with appeals, which might rehear the merits of a case. When the U.S. waste-disposal company Metalclad used Chapter 11 to attack the environmental order made by a Mexican village that had shut down its landfill site, the arbitrators, who met in Washington, ruled in the company's favour. Because the tribunal had named Vancouver as its nominal address, the Mexican government's only recourse was to the Supreme Court of British Columbia, which considered the review under B.C.'s provincial legislation providing for the review of foreign arbitral awards arising from commercial disputes.

For Canadian governments, the lack of an appeal process subverts the notion that the decision of a tribunal will ultimately adhere to the most fundamental notions of justice that have been woven into the fabric of its constitutional democracy. Because arbitral awards may be set aside for being incompatible with the legal norms of the state chosen as the place of arbitration, this may have the absurd result of having the courts of a nation with no connection to the dispute, assessing whether the award is consonant with its public policy — not that of the state defending its measure, or even the host state of the disputing investor. Yet this is precisely what occurred in the Metalclad case.

Transparency. Transparency is also a victim in the secret world of investor-state justice because commercial-arbitration proceedings, following the norms of commercial arbitration, are held in camera. The pleadings, evidence, and arguments may be kept secret if either party objects to their publication. The same is true for the award itself and, while NAFTA accords the parties the explicit right to release tribunal rulings, nothing requires them actually to do so.

Fairness. The notion of fairness to the interests of non-parties is entirely absent from the arbitral model. No provision for the participation of third parties is offered by either NAFTA's own clauses or the arbitration rules, which they invoke. While tribunals may accord a third party an opportunity to make submissions on public interest grounds — this is certain to be permitted only on the most restrictive terms (*UPS v Canada*, note 3).

Objectivity and independence. The sociology of the panellists' selection for international arbitral tribunals makes it highly likely that they will respond to the legal arguments privileging the norms of international commercial law at the expense of domestic values. Because the litigating investor and the defendant state each have the right to appoint one arbiter, and since the panel's chair is chosen by these two appointees, it is likely that there will be just one Canadian adjudicating suits launched against Canadian governments. This suggests that, when a norm of international corporate law comes into conflict with a Canadian legal standard, the latter is likely to be overridden.

Moreover, Chapter 11 cases are good business for the private international commercial judicial community that, as Dezalay and Garth (1996) have shown, has a vested interest in promoting the development of a largely autonomous Americanized and privatized global domain of corporate law. This situation raises questions about the self-interest of adjudicators' influencing the outcome of disputes. In the *Desona* case, for example, the tribunal found the disputing investors guilty of fraudulent conduct and their claim entirely lacking in merit, but it ordered no costs against them. Whatever the reasons for this ruling, it clearly sent a message to would-be disputing investors that they would not be penalized for launching even the most frivolous and unmeritorious of fishing expeditions.

The Lack of Reciprocity Increases Exposure to Investor State Claims Rights without Restraints. Unlike state-to-state procedures, NAFTA's Chapter 11 gives foreign investors substantial new rights without imposing on them any corresponding restraints or obligations. For instance, Chapter 11's new corporate rights were not balanced with a requirement to promote the public interest by protecting the environment or public health. Recourse to investor state litigation is untempered by many of the considerations — such as the fact that NAFTA disciplines also bind the complaining state — that intervene to limit state-to-state claims. The new system is also skewed because foreign corporations and their investors were given weapons that neither citizens nor domestic corporations enjoy to attack governmental regulations. Moreover, no balancing obligations have been imposed on them by continental-level institutions such as those developed in the European Union, which have the clout to regulate their behaviour, redistribute some of their winnings through taxation, or to monitor and adjust the workings of the emerging continental market (Blank and Krajewski 1995). Chapter 11's new corporate rights do not, for example, prescribe a requirement to promote the public interest by protecting the environment or public health.

Taken together, the factors described here cast a broad shadow over the landscape of domestic policy and law. Governments must now chart a course through the uncertain terrain of international trade disciplines, which may be invoked with few constraints by foreign corporations. The impact is to constrain the authority of Canadian governments at all levels as definitively, but more arbitrarily, than do the norms and limitations imposed by Canada's constitution and its common law.

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Investor Protection in NAFTA and Beyond:
An address delivered on September 28, 2001

Pierre S. Pettigrew

Thank you very much. I am pleased to join you all today for this very important discussion.

If you'll permit me, I'd like to begin by setting the context for this discussion. Sadly, this now requires saying a few words about the terrible events of September 11.

On September 11, North Americans were shocked to discover that our very security was being challenged. In the face of such sickening violence, we are still experiencing mixed feelings of grief, anger, and fear.

We learned that our institutions and our values are under attack by forces that went to unprecedented lengths to destabilize and terrorize all of western society. These events and this new realization have changed our perspective, our focus, and our priorities.

The past two-and-a-half weeks have been particularly challenging for our closest neighbours. They have suffered a tremendous and heart wrenching loss. To those of you in this room who may have experienced the direct loss of a family member, friend, or colleague, I extend my sincere condolences. I know that words simply cannot do justice to the painful losses some have experienced.

But, we know that the impact also extends far beyond those directly related to, or acquainted with, victims. Indeed, since September 11 it has seemed as if the entire continent, if not the entire western world, has been in a state of post-traumatic shock. We sense that the world will never be the same, though we hope that — somehow — it will emerge stronger, more united, and safer.

Aside from shaking our societies to their very roots, the horrendous events of September 11 have also demonstrated to us how fragile — and interdependent — our economic systems are. Isolationism is now virtually impossible; our interdependence is more obvious now than ever before.

In the months and years ahead, as we try to enhance security at our borders, in our airports, and throughout society, we must dedicate ourselves to achieving our goals without withdrawing behind our own respective borders.

Going forward in this climate, one of the most important elements will be open dialogue. And that is why I want to congratulate the C.D. Howe Institute and the Munk Centre for International Studies for their decision to combine their efforts in this way.

As a proponent of open dialogue, I think it is very important for members of both the business community and the academic community to come together in forums like this one. As someone who has spent some time in both these worlds, I know that each has a particular contribution to make to the policy-making process.

And make no mistake, this sort of gathering is an intrinsic part of the policymaking process. Exchanges like the ones we will have today can provide participants with information about the government's policy directions, and provide elected people like me with valuable insights into the concerns of my fellow citizens.

So by taking an active part in this initiative you are demonstrating a genuine civic spirit. I think it is fair to say that that spirit is embodied in the subtitle of the subject I have been asked to address today, which reads "private interest and public purpose."

Investor Protection in FTAs: The Need For Balance

The concepts of private interest and public purpose are also at the heart of investor protection, an important element in liberalized trade.

The two principles can seem at times to be at odds. As a result, the subject of investor protection — in NAFTA and in other free trade agreements — is a sensitive one.

Indeed, NAFTA's Chapter 11 has spawned more myths than ancient Greek theology, and has acquired a symbolic aspect that goes far beyond the reality of the situation.

Antiglobalization protesters have seized on it as the embodiment of an alleged confrontation between public and private interests, and more specifically between the broad public good and narrow corporate interests.

There is a perception among some citizens that Chapter 11 lets "private interest" trump "public purpose."

These perceptions need not persist; the public policy debate does not have to be framed in zero-sum terms, where public good suffers if private interests gain, or vice versa.

Underlying Chapter 11 are basic tenets that most Canadians firmly believe in. That governments should act prudently, not precipitously, especially when it comes to the property of citizens. That governments' decisions on the disposition of private property not be capricious, be fair, necessary, and constrained by the rule of law.

No one wants to see a person's home expropriated for a highway. Unless, of course, there's a compelling public policy need, and compensation is fair. Even then, Canadians would say that the home-owner should have the right to fight the decision within our legal system, if they choose to. Chapter 11 only seeks to capture that same sense of fairness and provide that same legal protection.

Canadians routinely invest in a mutual fund or buy stock in a company to prepare for their retirement, plan for their kids' education, or grow wealth and income. They have a right to expect these investments will be free of arbitrary or discriminatory government actions. It's reasonable to expect these companies will be treated evenhandedly, and will have the same opportunity as all other firms to grow and profit.

Of course, Canadians also expect their government to act in the public good. It is up to governments to ensure that private interests and the public good are considered in tandem, so that both sides benefit from the relationship.

As the Minister for International Trade, I am very committed to ensuring that "private interest" and "public purpose" are each reflected and protected in our investment rules. I believe such an approach will benefit everyone and make for stronger free trade agreements.

Why Trade and Investment Matter

That "benefit" should not be underestimated. After all, Canadians have gained a great deal from free trade and NAFTA. Since NAFTA came into force, trade, investment, and jobs have grown dramatically in Canada and throughout North America.

A clear set of rules for conducting international business is one of the key reasons for NAFTA's success. Clearly understood and mutually agreed trade and investment rules protect the flow of trade and investment capital, for everyone's benefit.

And, given that Canada is more "trade-focused" than any of our competitors, we clearly have a vested interest in keeping that two-way flow of trade and foreign investment strong.

For those Canadians who are concerned about the role of foreign investment in our economy, let me offer a few facts. Foreign investment helps ensure Canadian firms have the capital they need to succeed and grow in the highly competitive global economy.

Investment creates jobs and spurs innovation, by bringing new ideas and technologies to our companies. In short, investment provides Canadians with access to the capital and expertise that make our country stronger, and contributes to the quality of life of every citizen.

At the same time, there is also the issue of Canadian investment in foreign markets. Canadian investment abroad is equally important, as this helps Canadian firms establish a presence in foreign markets and share Canadian expertise, through the export of goods and services to those markets.

It should also be noted that yet another benefit is that a large proportion of profits from new investments is reinvested in Canada, contributing to a higher growth rate and a rise in Canadian living standards.

Benefits of Foreign Direct Investment

There is no doubt today that foreign direct investment — or FDI — in Canada and Canadian investment abroad have joined the international trade in goods and services to become our vital engines of growth and job creation.

In 2000, the stock of foreign direct investment in Canada reached a record $292 billion. To get a sense of what that can mean to the Canadian economy, consider that one OECD study shows that each $1 billion increase in new inward investment can generate up to 45,000 new jobs, and $4.5 billion in GDP.

And for those pessimists who might look at this good news and think that Canada is being bought up by foreign firms, let me reassure you with the following.

Canadian direct investment abroad is even stronger than foreign direct investment in this country.

Indeed, the value of Canadian direct investment abroad has increased by an astounding 400 percent between 1985 and 2000, from $57 billion to $301 billion.

Since 1997, the stock of direct investment abroad by Canadians has exceeded the stock of foreign investment in Canada. This reflects the maturity and wealth of the Canadian economy.

I should add that this type of investment results in increased sales and production from home facilities. A recent study by the OECD found that, on average, every $1 of investment is followed by $2 of exports. In other words, it all adds up to jobs and opportunities for Canadians.

Why We Need Rules

As you can see, investment and trade are inextricably linked. In fact, one inevitably leads to the other. And both are extremely important to our economic health.

That is why it is important for Canada — now, more than ever — to work toward achieving a fair, open, and secure environment for international investment, both at home and abroad. This is key to increasing our productivity and our prosperity.

The part of the North American Free Trade Agreement dealing with investment — Chapter 11 — ensures that investors are treated even-handedly. This chapter is an essential element of the agreement.

Now, here again, there are misconceptions surrounding Chapter 11, and I appreciate this opportunity to address them, and refute them.

To begin with, it is important to note that promoting investment in Canada has not jeopardized our main economic and social values. Foreign investors in Canada are subject to the same laws and regulations as are Canadian investors, including those aimed at protecting the environment, and those ensuring the highest labour, health, building, and safety standards.

Furthermore, I want to emphasize that our government's ability to set policy in the public interest on environmental, cultural, and social issues has not been compromised.

Clarifying the Rules

Both the public interest and the interests of individual investors are advanced by clear investment rules.

It is very important that investors be protected from arbitrary or discriminatory actions by governments. It is equally important that the ability of governments to regulate in the public interest not be compromised by unintended interpretations of investment rules. And, I believe that NAFTA appropriately reflects both these interests.

But, to some, Chapter 11's proceedings seem shrouded in secrecy and this raises doubts about whether the public interest is indeed seriously considered. In response to such concerns, I am pleased to say that my NAFTA colleagues and I recently confirmed the proper interpretation of two important aspects of Chapter 11.

As confirmed in the notes of interpretation we issued on July 31, 2001, each NAFTA partner will make available to the public virtually all documents submitted to, or issued by, Chapter 11 tribunals.

As well, it was reaffirmed that each partner can share all relevant Chapter 11 documents, including confidential information, with their respective federal, state, and provincial officials. This is obviously important as we work together with our provincial colleagues on issues relating to investment.

This clarification was a major step forward and, as someone who has dedicated himself to making the process as open and transparent as possible, I was very pleased that my American and Mexican colleagues and I were able to clarify these matters through our notes of interpretation.

A further issue addressed in the notes of interpretation of July 31 is the minimum standard of treatment to be accorded to foreign investors under NAFTA. We have reaffirmed that NAFTA's standard is the customary international law minimum standard of treatment.

Nonetheless, there remains more work to be done to ensure that Chapter 11 functions the way the drafters intend it to. We will, for instance, continue to work closely with our NAFTA partners to ensure that the provisions of the agreement are well understood.

I would also like to point out the role domestic courts can play in the operation of Chapter 11. We have asked the Federal Court of Canada to set aside a decision of a NAFTA tribunal in a case brought against the government by the firm S.D. Myers Inc.

We have also intervened in a statutory review of a NAFTA case brought against the Government of Mexico by an American firm, Metalclad. On May 2, 2001, the B.C. Supreme Court ruled that the tribunal had exceeded its jurisdiction in certain elements of its award. Although the award was not set aside in its entirety, the court did find that in several important respects the tribunal had overstepped the bounds of its authority. Canada will have to consider what form of participation is appropriate should appeals proceed.

I want investors' rights to be clearly stated and agreed upon and I want them to be properly interpreted. It is very important that investors' interests be protected in a rules-based system.

It is equally important that the ability of governments to regulate in the public interest not be compromised by unintended interpretations of investment rules.

As the July 31 notes of interpretation make clear, NAFTA recognizes this important balance. Furthermore, as we said at the time, the NAFTA partners will continue to work together to ensure that the public interest and the interest of investors are both advanced.

Investment Protection in Other Fora

Needless to say, the experience we have gained in our ongoing review of Chapter 11 will greatly benefit us in other trade negotiations. For example, in the case of the Free Trade Area of the Americas (FTAA), the issue of investor protection is at the early stage of negotiation.

In the FTAA, each participating country has the opportunity to submit proposals to the nine negotiation committees, one of which deals with investment. In August of 2001, Canada submitted a proposal concerning the minimum standard of treatment.

Our proposal would make clear that each party shall accord to investments of investors of another party treatment in accordance with the customary international law minimum standard of treatment of aliens, including fair and equitable treatment, and full protection and security.

This text reflects our experience with past trade agreements, including NAFTA.

At the WTO, there is no consensus at this time to move forward on investment. Nonetheless, at the next ministerial meeting, scheduled to be held in November of this year [2001] in Qatar, the question of investment protection may well come up.

However, irrespective of the course of action that is chosen by WTO members on the question of whether to include investment in a new round, rest assured that our government is committed to safeguarding Canada's right to regulate in strategic sectors, like health, education, culture, and environmental protection.

That is what Canadians have always wanted, and it will be what their government maintains and promotes.

Conclusion

Over the years, foreign investment in Canada has been an important source for jobs, especially high-skilled jobs, and has brought with it other advantages in research and development, new ideas and technologies, and talented people. These have all made real and lasting contributions to our economic and social well-being.

Yes, there have been disputes between governments and companies. There always have been and always will be. But these disputes tend to attract more public attention for the simple reason that they are rare.

When you contrast the small number of NAFTA Chapter 11 cases against the vast amount of trade that occurs — now over $1.9 billion a day with the United States and Mexico — it quickly becomes apparent that the few cases that have arisen in the past seven years are marginal compared to the broader trading and investment relationship. In 2000, our NAFTA partners together held $186 billion of investments in Canada.

Yet out of this large, growing, and important source of investment, and despite thousands of new laws and regulations passed by every level of government in Canada since 1993, we currently have only three active cases in arbitration against the Government of Canada under NAFTA, Chapter 11.

The fact is that disputes affect a very small portion of the billions in investment that Canada attracts and that Canadians invest abroad. We must not allow such minor irritants to detract from the many obvious benefits of trade. Now, especially after the tragic events of September 11, we must renew our commitment to an open, interconnected world.

We must reach out to other nations; strengthen the ties of trade and friendship, increasing the volume of exchanges of all kinds. And, we must not forget, as we approach Doha, that developing countries, in particular, can benefit from investment and investment rules. Such rules contribute to broader efforts to strengthen investment climates in developing countries and to attract the private capital needed to spur their economic growth and development.

The importance of rules is, in fact, being highlighted in the broader context of UN Financing for Development discussions on "mobilizing international private resources for development."

Investment protection is thus a critical element of a rules-based trading system that has the potential to enrich those who take part. Let us all work together to build such a rules-based trading system on a worldwide level, for the benefit of all people.

Defining and Pursuing Canada's National Interest

Stephen Brereton

One of the key objectives of the Government of Canada is the promotion of prosperity. From a trade and foreign policy perspective, we can accomplish this by fostering the expansion of Canada's international trade and economic interests abroad. It is also essential to secure market access for Canadian goods and services by providing a competitive environment through the import of ideas, goals, services, and capital to be combined with Canada's human and other resources, by promoting foreign investment into this country, and by encouraging Canadian investment abroad.

Today's globalized economy is increasingly based on the more intangible output of service firms and is to a large extent dependent upon international capital flows. One fundamental characteristic of this new economy is that it relies more and more on the creation, purchase, and transfer of capital and knowledge. In addition, the increasing importance of positioning within global value chains has increased competitive pressures — and opportunities — for Canadian firms in the marketplace.

Capital flows worldwide have grown rapidly in recent years — far faster than trade during the 1980s and 1990s — and have contributed to global economic integration. The global stock of outward foreign direct investment (FDI) has increased more than tenfold over the past two decades, from US$590 billion in 1982 to US$8.2 trillion in 2003 (UNCTAD 2004). Canada is an active participant in the global economy. The stock of Canadian direct investment abroad has nearly quadrupled from C$98 billion in 1990 to C$399 billion in 2003 (Canada 2004). Over the same period, the stock of foreign direct investment in Canada more than doubled, from C$131 billion to C$357 billion. Since 1997, the stock of Canadian direct investment abroad has surpassed the stock of foreign direct investment in Canada, reflecting the maturity of the Canadian economy.

As indicated in Canada's annual State of Trade Report, tabled in the House of Commons on May 2, 2002:

> Canada attracted C$42.8 billion of new foreign direct investment in 2001, a new record high, especially gratifying in view of the marked decline in mergers and acquisitions from the year before. Also, Canadians invested a near record high level of new direct investment abroad of C$57.3 billion last year, reflecting the dynamism and optimism of Canadian investors in a difficult world economic environment. (Canada 2002)

These dramatic changes reflect the fact that Canadian businesses know that if they are to prosper, they must compete internationally. Many Canadian companies not only have markets in other countries but also have established production facilities abroad through international investment or have established a commercial presence in foreign markets to supply their services. Other companies have significant minority or majority foreign ownership within Canada. International investment is thus becoming a central element in the business repertoire needed for success in today's global economy.

Inward and Outward Investment Flows: Positives for the Canadian Economy

Foreign direct investment in Canada contributes to the creation of jobs at home, often higher paying and higher skilled ones, and is an important source of economic growth. Further, most current research shows that FDI spurs innovation by bringing new ideas and technologies to our companies, provides much needed additional capital, and contributes to raising exports. Such investment makes our country economically stronger and contributes to a higher quality of life for all Canadians.

The positive link between Canadian direct investment abroad and exports is noted in an Organisation for Economic Co-operation and Development (OECD) study of 14 countries (Fontagné 1999), which estimates that, over the short term, each new dollar invested abroad results in two dollars of additional exports. When spread over several years, the effect on exports of new investment flows in developing countries can become three to four times the original investment amount.

Outward investment also plays an important role in promoting Canada's interests. Canadian direct investment abroad creates jobs abroad and at home. It strengthens the commercial links between countries by establishing a presence in foreign markets, which leads to increased profits, royalty payments, and other benefits, while sharing Canadian expertise through the export of our goods and services. In sum, cross-border investment plays an important part in the well-being of the Canadian economy and contributes significantly to the prosperity of Canadians.

Why Canada Pursues Investment Agreements

Because of the important contribution made by international investment to the economies of all countries, it is not surprising that governments are increasingly establishing the national policy frameworks necessary to create an attractive investment environment. For many countries, this has involved simplification or abolition of investment screening mechanisms, easing of sectoral investment restrictions, and opening entire sectors to foreign investment through privatization programs. Frequently, these domestic efforts to improve the investment climate have been augmented by international agreements that confirm, at the international level, the positive changes to their foreign investment policy regimes.

The desire of governments to facilitate freer flows of international investment through international rulemaking in this fashion is reflected in the dramatic increase in the number of bilateral investment treaties (BITs) in the 1990s. These were designed to provide predictability, protection, transparency, and access for investors in specific priority and emerging economies. While there were fewer than 400 BITs at the beginning of the 1990s, by 2003, this total had surpassed 2,200 bilateral agreements. Canada is currently party to 22 ratified BITs, also called foreign investment protection and promotion agreements (FIPAs).

When it comes to pursuing investment rulemaking, countries have also been active at the regional and multilateral levels. Canada negotiated both the Canada-U.S. Free Trade Agreement and the North American Free Trade Agreement (NAFTA), which established rules on investment. Canada also has a free trade agreement with Chile (the Canada-Chile Free Trade Agreement (CCFTA), which entered into force in 1997), which includes an investment chapter, Chapter G that follows the model found in NAFTA Chapter 11. Shortly after NAFTA came into force, the OECD member countries attempted, unsuccessfully, to develop a "high standard" multilateral agreement on investment (MAI). Rules respecting investment are part of the negotiations toward the Free Trade Area of the Americas (FTAA).

With a lack of success at the multilateral level, focus has shifted to bilateral efforts. Canada has developed a new model FIPA and has commenced a renewed bilateral FIPA program. As of 2004, negotiations were underway with Peru, China, and India. Also in 2004, Canada initiated exploratory talks with South Korea towards negotiating a free trade agreement.

Typically, investment rulemaking efforts are focused on improving the conditions under which investments are made and include the principles of:

- *Transparency* — the provision of open reporting and publishing of national investment measures and rules and relevant regulatory changes to enable investors to have a clear understanding of the rules of the game;
- *Non-discrimination* — through national treatment and most-favoured-nation (MFN) treatment of foreign investors and their investments in host countries;
- *Protection* — investments and investors should be protected by ensuring fair and equitable treatment in accordance with customary international law standards for treatment of aliens,

compensation in the event of expropriation and free cross-border transfer of funds; and
- *Dispute settlement* — the provision of binding dispute settlement procedures to settle disputes arising from alleged breaches of the obligations taken by the parties.

As a medium-sized and open economy, Canada has supported these principles over the past 50 years in the international trade and investment areas. From the standpoint of investment, rules on transparency and non-discriminatory treatment play an important role in protecting and facilitating the foreign investment activities of Canadian firms by ensuring a stable, transparent, and predictable environment for international investment. This is what Canada has promoted in numerous international negotiations, including NAFTA, CCFTA, and the bilateral FIPA program. The rules within NAFTA, the CCFTA, and FIPAs provide a framework of disciplines, and encourage efficient resolution of disputes and greater consistency in legal and policy regimes. These rules also offer a greater measure of security for Canadian investors through assurances that national policies will not be changed unduly or applied in a discriminatory manner.

Investment agreements, while providing certain guarantees to investors and covered investments, do not restrict a country's ability to regulate in the public interest. Foreign investors in Canada (and Canadian investors in foreign markets) must abide by the domestic laws of the host country and obey the same rules as nationals. For example, foreign investors are neither exempt from domestic competition laws nor from regulations relating to health, labour, or protection of the environment.

Canada has a relatively open investment regime, which compares well internationally. Under the *Investment Canada Act*, foreign acquisitions of large Canadian companies are subject to review. For World Trade Organization (WTO) member countries that means companies with assets worth more than C$237 million. The threshold is modified annually, based on a formula taking into account changes to nominal gross domestic product (GDP) at market prices. Foreign investments in certain sensitive sectors, such as cultural industries, are also subject to review. Remaining investment restrictions in Canada lie largely in the services sector, for example, financial services and transportation. Restrictions in this sector are quite common and are found in many other countries including the United States.

Canada has long been a supporter of a rules-based trade and investment system (where agreed rules regulate the flow of goods, services, and investment) rather than a power-based one (where economic or military might dictate results), with the objective of bringing the investment regimes in other countries to Canada's level of openness. Indeed, investment rules promote values important to Canadians: that governments, while mindful of public well-being, act in a non-discriminatory manner, prudently, and not precipitously, when it comes to the property of investors, as they do in the case of citizens, and that governments' decisions on the disposition of private property not be capricious, but fair and constrained by the rule of law. These principles apply in Canada, and we want to make sure that they will be applied in the countries with which we negotiate such agreements, to protect Canadian investors and their investments. No one wants to have their property expropriated, but when there is a compelling public policy need to do so, one should be entitled to fair treatment and adequate compensation. Chapter 11 of NAFTA, and other similar investment agreements, seek only to capture that same sense of even handedness. Because Canada now invests more abroad than it receives in foreign direct investment, such protections are all the more important to Canadians.

Effective dispute settlement mechanisms are essential to ensuring that obligations undertaken in trade and investment treaties are respected. This may be accomplished through traditional state-to-state dispute settlement. Alternatively, the investor-state dispute settlement mechanism offers foreign investors another mechanism to seek redress for alleged damages suffered as a result of breaches of the obligations in international treaties. Investment rules thus promote the flow of capital by providing protections that mitigate risk and, in doing so, serve Canada's interests.

Canada's Experience with Investor Protection

Governments have long recognized the need to protect the rights of investors. However, the protection of investors in international agreements has come under criticism in Canada over the past few years. One reason for this appears to be the inclusion of a procedural mechanism never before included in a free trade agreement, namely the investor-state dispute settlement mechanism in NAFTA. Although often viewed as new, such a mechanism was included in the FIPAs and many other bilateral international treaties, signed prior to NAFTA.

Since the implementation of NAFTA, four cases involving the Canadian government have led to the establishment of an arbitral panel under Chapter 11, one of them was still pending in 2004. All four cases against Canada were launched by U.S. investors. There have been no cases between Mexican investors and Canada. Also, ten Canadian investors filed claims against the U.S. government.[1] As of late 2004, there was a case between a Canadian investor and Mexico (see Canada 2004b).

In the debates that have surrounded Chapter 11 cases, some have raised the issue of the balance between private interest and public purpose. Some of the concerns put forward result both from the way the arbitrations were conducted and from the substantive issues that were at the centre of the claims. Each of these is addressed in turn below.

The Arbitral Proceedings and Transparency

NAFTA stipulates that Chapter 11 proceedings shall be conducted in accordance with the International Centre for Settlement of Investment Disputes (ICSID) Rules, ICSID Additional Facility

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[1] Although as of June 2, 2005, members of the Canadian Cattlemen for Fair Trade have filed 107 individual Notices of Arbitration alleging that the United States has violated its NAFTA Chapter 11 obligations by closing the border to importing Canadian cattle, all these Notices deal with the same underlying claims and are collectively considered to constitute only one of the 10 claims filed by Canadian investors against the U.S. government.

Rules,[2] or the United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules, except as modified by Chapter 11. So far, in cases against Canada, claimants have elected that proceedings be conducted under the UNCITRAL Arbitration Rules. Proceedings brought under the investor-state provisions of NAFTA's Chapter 11 have often been characterized as excessively secretive and closed, and some question the appropriateness of closed hearings when government measures are at issue. To address such concerns, Canada has been working closely with its NAFTA partners to make the investor-state dispute settlement process as open and transparent as possible.

An important milestone in Canada's efforts to enhance transparency in the NAFTA dispute settlement process occurred on July 31, 2001, when the NAFTA Free Trade Commission (FTC) reaffirmed that, subject to certain limits, each NAFTA partner would make available to the public all documents submitted to, or issued by, Chapter 11 tribunals. NAFTA governments may also share all relevant Chapter 11 documents, including confidential information, with their respective federal, state, and provincial officials (NAFTA 2001). Canada was the first NAFTA partner to make documents related to its Chapter 11 arbitrations public on its website (Canada 2004b). The United States and Mexico have followed Canada's example and created websites of their own that contain documents related to Chapter 11 cases.

During their meeting in October 2003, the NAFTA Free Trade Commission (FTC) issued a joint statement outlining a recommended set of procedures for tribunals to follow when deciding who should be permitted to make amicus-type written submissions during an arbitration. The procedures closely follow recommendations from a joint committee of the Barra Mexicana, American Bar, and Canadian Bar associations. This statement indicates a commitment from the three NAFTA governments to greater participation of companies, trade associations, and other non-governmental organizations (NGOs) in the arbitration process.

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[2] That is, if either the disputing party or the party of the investor, but not both, is a party to the ICSID Convention.

In addition to this joint statement each NAFTA party has also issued individual policy statements of their own on the subject of open hearings in Chapter 11 arbitrations. All three governments affirmed their commitment to open hearings in Chapter 11 arbitral proceedings to which their government is a party and pledged to request that disputing investors also commit to open hearings. This is a significant enhancement to the transparency of the Chapter 11 dispute settlement mechanism.

In July 2004, the FTC took a further step to enhance the transparency of Chapter 11 by releasing the draft negotiating texts of Chapter 11. These steps serve to increase public understanding of the operation of Chapter 11 and help the NAFTA parties in building better and more transparent rules for future international trade agreements. The enhancements in the NAFTA context have been taken up as the new world standard for transparency in such agreements. For example, the membership of ICSID is currently considering changes to their dispute settlement rules that closely resemble the transparency enhancements developed by the NAFTA parties.

Canada has been at the forefront of efforts to promote transparency in a variety of international forums, including NAFTA and the WTO. This is a record of which Canada is justifiably proud. Canada's commitment to transparency in the conduct of international trade does not stop there. For example, Canada's initiative also resulted in the 34 trade ministers responsible for the negotiation of the FTAA agreeing to release the draft text of the negotiations in the spring of 2001.

The Regulations at the Centre of the Claims

Critics of NAFTA's Chapter 11 are concerned over the right and ability of governments to regulate in such substantive areas as the environment. Chapter 11 expressly affirms the ability of countries to adopt and enforce measures that they consider appropriate to ensure that investments "are undertaken in a manner sensitive to environmental concerns" (NAFTA Art. 1114(1)). Since the implementation of NAFTA, there have been more than 40 environmental regulations put in place by the Canadian government. Also interesting, these environmental regulations were only partly implemented under acts administered by Environment Canada; the others were initiated under acts administered by other federal departments, which illustrates that environmental considerations are omnipresent in policymaking. In addition to the regulations noted, several legislative initiatives, including the *Migratory Birds Convention Act*, the *Alternative Fuels Act*, the *Canada Marine Act*, the *Mackenzie Valley Resource Management Act*, and the *Oceans Act* have been put forward.

Regarding the authority of tribunals, it is important to note that, contrary to some state-to-state dispute settlement mechanisms, a Chapter 11 tribunal may only award monetary damages, costs and interest, and restitution of property (NAFTA Art. 1135). It cannot ask a party to modify its existing legislation, and it cannot award punitive damages. Tribunal awards are based on a breach of the Chapter 11 obligations between signatory states, and a breach of obligations is based on a tribunal's finding that a government has acted contrary to the Chapter 11 obligations of NAFTA — for example, on expropriation. This meets one of the goals of NAFTA's Chapter 11, which is to protect investors against expropriations and discriminatory actions of foreign governments.

NAFTA Governments' Initiative — the Clarification Exercise

Over the past several years, the NAFTA parties have been engaged in an ongoing review of Chapter 11 provisions and have collaborated to identify areas for clarification of key procedural and substantive provisions. As previously noted, in July 2001, the NAFTA FTC issued Notes of Interpretation which, in addition to reaffirming the importance of transparency, also addressed the interpretation of the minimum standard of treatment obligation contained in Article 1105. The FTC clarified that Article 1105 refers to the customary international law for minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another party. In addition, the interpretation made clear that a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1) (NAFTA 2001).

The commitment of the NAFTA parties to review the operation of Chapter 11 continues. Recently, the FTC directed officials from the three parties to continue their work seeking ways to further improve the implementation of Chapter 11, including through, where appropriate, an examination of the experiences of the NAFTA parties in subsequent free trade agreements, which have been negotiated.

Government Initiatives — Consultations with Canadians

Because of the importance of these issues and the range of views held in Canadian communities, it is vitally important that the government consult widely and regularly. Government officials are committed to do so.

International Trade Canada has a specific section on Chapter 11 on its website, where it posts information of interest. In addition, publicly available information concerning all Chapter 11 cases is being continually added. The objective is to develop material that will address the needs of a varied audience, for instance business people, lawyers, the NGO community, and the general public. Ideas on how we can improve the website and general input on policy matters are always welcome. These can be sent to consultations@dfait-maeci.gc.ca.

The Government of Canada also consults in many other ways, both internally and externally. One of the government's basic means of consultation is its regular quarterly C-Trade meetings, where federal, provincial, and territorial representatives address outstanding issues, including those that have arisen from the operation of Chapter 11. There are also regular interdepartmental meetings of federal government officials to further analyze the workings of investment rules, taking into consideration the input from the various consultative initiatives.

International Trade Canada is also engaged in extensive discussions with Canadian municipalities, through the Federation of Canadian Municipalities (FCM). These meetings give municipal representatives direct access to trade negotiators and technical experts in the federal government. The FCM representatives seek and receive clarification on the relationship between international trade agreements and their areas of responsibility in addition to gaining a better understanding of the benefits to be obtained from international trade agreements. This International Trade Canada – FCM working group is currently engaged in developing a manual that will provide municipalities across Canada with a clearer understanding of these issues.

International Trade Canada, as well as Finance Canada, Environment Canada, and various other government departments, are working closely together to foster discussion and debate, identify issues, and address them. One of these initiatives is the creation of an ad hoc experts group on investment rules, which meets periodically. The backgrounds and experiences of the members of the group vary, and represent various viewpoints in the community. The small group is composed of academics and lawyers, as well as industry and labour representatives, and it analyzes issues in depth, trying to define avenues of action.

Another initiative was the Chapter 11 workshop, which was organized in January 2002 by the Centre for Trade Policy and Law (CTPL) in Ottawa and sponsored by the then-Department of Foreign Affairs and International Trade, Industry Canada, and Finance Canada. The proceedings were published in Dawson (2002).

Officials from the NAFTA parties tasked with reviewing the operation of Chapter 11 decided to seek stakeholder views on Chapter 11 to assist and inform their work in developing recommendations for the FTC. Canada hosted a trilateral, multi-stakeholder consultation in Montreal on May 28, 2003 (Canada 2003b). This important event was followed in October 2003 with a larger multi-stakeholder consultation organized as part of the *NAFTA@10* activities hosted by Canada at the FTC meeting held that year in Montreal (Canada 2003a).

Conclusion

These observations hopefully give the reader a sense of the work the Government of Canada is doing to address issues arising in the operation of Chapter 11, in addition to how and with whom it is looking into these issues. I would like to conclude with two thoughts. First, in assessing how well the investment rules we have put in place work, one has to keep in perspective that, for the billions of dollars of cross-border trade and investment that have flowed in the more liberalized North American market since NAFTA came into force, only a very limited number of investors have brought a complaint pursuant to Chapter 11's provisions. And second, it is important to emphasize that Canada will not yield its right to set its own laws and regulations to protect the health and environment of its citizens. Canada will continue to support the complementarities of trade and social services, health, public education, and environmental policies, including ensuring the proper balance of public purpose and private interest in future international investment agreements.

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A Commentary on Defining and Pursuing Canada's National Interest

Gilbert R. Winham

Chapter 11 of NAFTA was widely regarded as a major investment agreement when it was signed in 1993 and the passage of time has only confirmed that judgment. Steve Brereton has written a valuable summary and overview of the Chapter 11 process, and noted especially how Canada and its NAFTA partners have responded to such issues as transparency that have arisen in the implementation of the agreement. The paper is a valuable reminder of the importance of investment to Canada, both inward investment, which traditionally has played a role in the economic development of the country, and outward investment, which is important in continuing the growth of the country's exports. Chapter 11 is essentially an effort to establish the rule of law in investment policy, and it is of particular importance to medium- and small-sized investors. The motivation behind the agreement is not so much to provide for the rule of law for the investors from other countries, but to encourage other countries to provide the rule of law for outward investors, and it is clear that there cannot be one without the other. The creation of reciprocal rights is the basis of international economic agreements, and indeed it is the basis of all legal commitments, foreign and domestic.

The main issue arising from Chapter 11 is its implementation through the dispute settlement system built into the Chapter. That is because in any rules-based system, implementation through dispute settlement is where the rubber hits the road. Brereton's paper provides some analysis on this matter, but in my view there is more to be said.

Dispute settlement in Chapter 11 is provided through an investor-state mechanism, which was considered unique and innovative when it was established during the NAFTA negotiation. After a slow start, investors began to challenge regulatory policies that they said had discriminatory and negative impacts on investors' interests. By the beginning of 2002, 21 complaints had been filed under Chapter 11, of which only five led to arbitral decisions; the remaining cases were settled, withdrawn or were in process.[1] Of the five completed decisions, three returned awards to the claimant-investor (*Metalclad* v. Mexico, and *S.D. Myers* and *Pope and Talbot* v. Canada) and two dismissed outright investors' claims (*Azinian* and *Waste Management* v. Mexico). These various cases raise two important debates. The first is whether Chapter 11 should be applied to the general actions of governments.

One variant of this debate holds that foreign investors are private parties and, as such, should not have the legal capacity to challenge actions of governments, which in turn represent the sovereign will of a people. This view is held by some environmental non-governmental organizations (NGOs), as well as by the Council of Canadians, and it leads to the conclusion that Chapter 11 (and indeed NAFTA itself) was a bad idea from the outset, which is only confirmed by the cases now being brought against governments. This position is not supported by the Government of Canada, nor should it be.

Another aspect of this debate is whether Chapter 11 should have jurisdiction over laws or regulations other than those that explicitly govern foreign investment. This issue was raised in *Ethyl Corp.* v. Canada, the first case under Chapter 11. It is useful to review the facts of the case. In 1997, Canada passed the *Manganese-based Fuel Additives Act*, which prohibited inter-provincial trade and importation into Canada of MMT, a fuel additive designed to increase the efficiency of unleaded automotive fuel. One company, Ethyl, manufactured MMT in the United States and a wholly owned subsidiary widely distributed it in Canada. Auto manufacturers claimed that MMT interfered with mandated pollution control devices in vehicles, but Ethyl disputed this claim. (Soloway 2002). The Canadian government claimed the Act was an environmental measure, though the government failed to find evidence that MMT was harmful, and the Act itself only banned trade in MMT; it did not prohibit the production and distribution of the product in inter-provincial commerce. Arguably, the Act would have permitted or even encouraged Ethyl to establish production facilities in each of the Canadian provinces as a means to service the Canadian market.

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[1] For an up-to-date listing of complaints and decisions under NAFTA Chapter 11, see Table 1 in the volume's concluding chapter.

Ethyl brought an arbitration under NAFTA Chapter 11 claiming that the Canadian Act constituted a denial of national treatment and was an action "tantamount to expropriation" under Article 1110(1) of NAFTA. In turn, the Canadian government argued that the tribunal lacked jurisdiction because Chapter 11 was only intended to deal with laws directly related to investments, such as foreign investment review legislation, and not to regulations drafted for more general purposes. The tribunal largely rejected Canada's jurisdictional claims.

The tribunal never rendered a judgment on the merits of the case because the parties settled the dispute, and the Canadian government rescinded the Act and paid Ethyl C$19.3 million. The motivation for the government's action was a decision by a dispute settlement panel which had been initiated by Ethyl under Canada's Agreement on Internal Trade (AIT), an agreement between the federal and provincial governments, designed to promote freer trade within Canada. The panel found that the Act violated the Agreement because it restricted the movement of goods across provincial boundaries (Article 402) and operated to create an obstacle to internal trade (Article 403), and could not be saved under Article 404, which provided for exceptions to the requirements of Articles 402 and 403 for "legitimate objectives". The panel decision was an embarrassment for the federal government that had championed the AIT in the first place.

In *Ethyl*, Canada in preliminary argument took the position that NAFTA Chapter 11 was not intended to have jurisdiction over so-called environmental acts, but only over laws directly related to foreign investment, such as legislation to review or regulate foreign investors. The Tribunal rejected this argument, though in retrospect this position seems defensible. In the NAFTA annexes that list the exceptions to which Chapter 11 rules do not apply, the laws that are listed are clearly diverse. It seems clear that the NAFTA Parties took the position that any law that had provisions affecting foreign investment should be listed if exceptional treatment were sought, which suggests that laws did not have to be mainly directed toward foreign investment to be affected by Chapter 11. The upshot of the *Ethyl* jurisdictional decision, and similar decisions in other cases, is that Chapter 11 applies broadly to government legislation. As a result, governments cannot accept a treaty that provides rights for foreign investors, while taking away those rights through domestic legislation that ostensibly serves purposes other than regulating foreign investment.

The second debate is that if NAFTA Chapter 11 is a good idea, and if it applies broadly, were there nevertheless mistakes made in the drafting that need fixing? Particularly, issues have been raised about whether Chapter 11 provided too much scope for claims by foreign investors, and possibly even more than for equivalent claims by domestic investors. These questions tend to focus on Article 1110(1) on Expropriation and Compensation, which reads as follows:

> 1 No Party may directly or indirectly nationalize or expropriate an investment an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ('expropriation'), except:
>
> a. for a public purpose;
> b. on a non-discriminatory basis;
> c. in accordance with due process of law and Article 1105(1); and
> d. on payment of compensation in accordance with paragraphs 2 through 6. (NAFTA 1994)

One issue to be raised is that the phrase "tantamount to expropriation" goes beyond the language of expropriation in domestic law, and therefore provides for better than national treatment for foreign investors. On this matter, Canada requested an Interpretation by the NAFTA Parties, which was opposed by Mexico on the grounds that the Parties should first wait for results from the arbitral process. Two panels (*Pope & Talbot* and *S.D. Myers*) have now rendered decisions on this question, and have reached the rather common-sense conclusion that "tantamount to" means "equivalent to", and that something equivalent to something else cannot be less than it. The less excited Mexican approach to this matter appears to have been confirmed.

A second issue is the definition of expropriation. The issue, as raised by environmental groups, concerns government regulations that allegedly create a small loss of value, such as a loss of market share: should a government be required to pay compensation in such a case? This issue was addressed in the U.S. Senate in the Kerry Amendment to the Trade Promotion Authority bill — fast track legislation. The Kerry Amendment would have specified that compensation is not required for government measures "that cause a mere diminution in value of private property." The amendment was successfully opposed on the grounds that expropriation is very hard to define operationally, it is fact-specific, and should be defined in the context of actual cases.

A third issue deals with the protection for governments from frivolous suits by foreign investors. This is a reasonable concern, especially because Chapter 11 has a wide-ranging definition of investment that could give rise to claims that go beyond what might reasonably be regarded as legitimate. Furthermore, this issue arose in the first case under Chapter 11 arbitration (*Azinian v. Mexico*) where the panel dismissed the complaint and likely would have awarded damages to the Mexican government but for the novelty of the proceedings. There were indications that officials in the United States were looking at proposals that would deal with frivolous suits by providing for an expedited review by panels on whether or not the panel had jurisdiction. In cases where the parties brought suits dismissed as frivolous, those parties would be assessed costs for the government and for the administrative expenses associated with the panel. Such procedures would be a reasonable deterrent to parties with marginal claims. The important thing is that governments themselves should not have the power to dismiss cases as frivolous because governments are parties to the action. Instead, this power should be left to the arbitrators themselves, or to some third party.

A fourth issue deals with appeals from Chapter 11 panels. There is probably a good case for establishing an appellate procedure in Chapter 11 because there is a disturbing variability of findings in the arbitral awards of some completed cases. This likely happens because expropriation is inherently difficult to define operationally — it has a problematic history in both international and domestic law. There is a tendency for some NGOs to see the variability of one panel's decision from another's as a potential assault on the sovereignty of governments by unelected international tribunals. As a result, it is important to recall that panels only have the power to award compensation to claimants in a single case, not to order changes to national laws. Still, it is important to get consistency and predictability in judicial rulings and it may be desirable to build in some form of appellate procedure in Chapter 11 procedures.

One U.S. proposal was to provide parties to a dispute with an opportunity to comment on an interim ruling from arbitrators prior to receiving a final ruling. An interim ruling would also allow the countries subject to an agreement to determine if they were in accord on the arbitrators' basic interpretation of the relevant provisions of the settlement. If there were doubts, the countries could agree on an interpretation that would bind the arbitrators. This procedure has been explored in the context of regional agreements such as the Free Trade Area of the Americas (FTAA), but it could be included in NAFTA in lieu of a more formal appeals process. This would avoid problems that surfaced in *Pope & Talbot v. Canada*, where arbitrators reached an interpretation of Article 1105 (Minimum Standard of Treatment) that was subsequently repudiated in an Interpretative Note issued by the NAFTA Trade Ministers operating under the Free Trade Commission (MacNeil 2002).

Another procedure for appellate review that is now being undertaken is appeal to national courts. This was done in *Metalclad v. Mexico*, where Mexico considered the arbitral award so flawed that it brought a petition to the Supreme Court of British Columbia, the competent court of the site of arbitration. The same procedure was followed in *S.D. Myers v. Canada*, where Canada sought review of the arbitral award from the Federal Court of Canada. The latter case is complicated, and it is useful to outline it briefly.

In 1990, Canada issued the PCB Waste Export Regulations, banning export of PCBs to all countries except the United States. These regulations permitted export of PCBs to the United States only by prior consent of the U.S. Environmental Protection Agency (EPA), which was granted only to U.S. government agencies operating in Canada. In 1995, the EPA granted S.D. Myers — a U.S. corporation engaged in PCB waste disposal, with a principal facility in Ohio and a branch in Ontario — permission to export PCB waste from Canada for disposal in Ohio during the period November 1995-to-December 1997. The EPA grant of permission to Myers was reversed by a decision of the U.S. Court of Appeals of the Ninth Circuit in July 1997. Because U.S. regulations would no longer be preventing the import of PCB wastes from Canada after 1995, the Canadian government took a series of measures between 1995 and 1997 that restricted the export of PCB wastes to the United States.

S.D. Myers claimed that Canada's PCB measures closed the border to its exports for over 14 months in violation of Articles 1102 (National Treatment), 1103 (Most Favored Nation Treatment), 1105 (Minimum Standard of Treatment), and 1110 (Expropriation). The company argued that the purpose of the PCB Measures was to support the only alternative Canadian PBC disposal facility in Swan Hills, Alberta, which in any case was more distant from Ontario and therefore not able to provide the service of the Ohio plant. For its part, the Government of Canada claimed the PCB Measures were environmental regulations taken pursuant to the Basel Convention on the Control of Trans-boundary Movements of Hazardous Wastes and their Disposal of March 22, which arguably could require Canada to dispose of its PCB wastes in Canada. However, under the Canada-U.S. Trans-boundary Agreement, Canada is under obligation to permit the export of PCBs.

The S.D. Myers case represented a complex overlapping of issues and jurisdictions. In its decision, the tribunal found that the

PCB measures were imposed in order to develop a long-term capacity in Canada for hazardous waste disposal, ostensibly a goal consistent with the Basel Convention. However, the method it had chosen was to place a discriminatory export ban that itself could not be justified on environmental grounds and that had the primary effect of protecting a Canadian competitor from foreign competition. As a result, the tribunal ruled unanimously that the PCB actions were inconsistent with Canada's obligations to provide national treatment under Article 1102 of NAFTA. On other matters, namely Articles 1105 (Minimum Standard of Treatment) and 1110 (Expropriation) the case went in favour of Canada. The Tribunal ordered Canada to pay about $8.2 million in compensation, which Canada took to judicial review (Chase 2002).

It is questionable whether judicial review is a good tactic. In the first place, the purpose of Chapter 11 was to ensure a certain minimum standard of treatment that foreign investors from the NAFTA area would receive from the NAFTA Parties. This treatment was outlined in the provisions of Chapter 11 and backed up by a dispute settlement process that insured investors could pursue their rights in an international arbitral process. If the results of that process are to be subject to review by national courts, the guarantees of Chapter 11 will be greatly diminished. For example, would Mexican investors in Canada feel secure if an arbitral award could be set aside by a Canadian court, or conversely, would Canadian investors in Mexico feel the guarantees provided by Chapter 11 were assured if Mexican courts were empowered to review the investor-state dispute settlement procedures of the NAFTA? Or, knowing that national judicial review would be brought to the competent court in the site of arbitration, would this lead the NAFTA Parties to contest the location of arbitral proceedings in which their governments are involved? There is a real concern that the provision of national judicial review in Chapter 11 cases will undercut the perception of the rule of law that was established in the investor-state procedures in the first place.

A second question is whether domestic judicial review is a good tactic for Canada. In considering this issue it is interesting to compare Canada's position in NAFTA Chapter 19 with its current practice in Chapter 11. Chapter 19 is the unique dispute settlement mechanism which provides for bi-national judicial-like review of disputes over anti-dumping and countervailing duties. It was an essential element in Canada's support for the Canada-U.S. Free Trade Agreement and, later, NAFTA. Chapter 19 explicitly specifies that bi-national panels will make a final decision which cannot be further reviewed in the courts of signatory countries. Canada insisted on this provision because it recognized that judicial review by domestic courts of bi-national panels could undermine the panel process, particularly if done by the United States. This could neutralize and render ineffective an internationalized dispute settlement mechanism.

There are similarities in the impact that domestic judicial review would have on Chapter 11 or Chapter 19 dispute settlement processes. In either case, the effect would be to weaken international dispute settlement and to strengthen the power of domestic decision making. In trade, Canada's traditional position as a middle power has led it to pursue the rule of international law, and to support institutions that promote a rules-based as opposed to a power-based process for settling disputes over trade rules. This concept has been extended to private investors by Chapter 11, and Canada supported the rules and investor-state dispute settlement mechanism of Chapter 11 because of the rapidly-growing interests the country had in outward investment. If other countries follow Canada's example in S.D. Meyers of seeking domestic judicial review of Chapter 11 arbitrations, then Canadian investors in the United States or Mexico will have to expect similar treatment in any disputes that might arise with the governments of those countries.

In this arrangement Canada loses two ways: first, in comparison to the United States, Canadian foreign investors are likely to be smaller and therefore in greater need of a stable international investment regime; and second, in comparison with Mexico, the Canadian judicial system which Mexican investors would face has a better reputation for the evenhanded dispensing of justice than does the Mexican judicial system, which would be faced by Canadian investors. In its effort to put matters right in a single case, the current Canadian government may have compromised an important principle that Canadian trade policy has fought for in the past.

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NAFTA Chapter 11:
Canada's Weakening of the International Rule of Law in the NAFTA Zone

By Ian A. Laird

Canada remains in the midst of its largest trade dispute ever with the United States over softwood lumber.[1] While fighting against aggressive U.S. unilateralism on one front, Canada has appeared to be capitulating to U.S. designs to reduce investment protections in NAFTA on another front. Yet Canada relies on the international rule of law to provide the moral authority it needs to confront its more powerful friend.[2] The international rule of law is a critical element in a rules-based system — a key Canadian trade policy objective.

For the United States, its principled reliance on the rule of law advocated following its founding has now evolved with its economic and military might into a form of à la carte multilateralism on the modern world stage. It means frequently that powerful domestic interests dictate whether the U.S. is prepared to comply with international law. While still supporting in principle a rules-based international system, including U.S. adherence to international law, in practice U.S. policy too frequently advances its own national sovereignty and reinforces a power-based global economic policy.

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[1] After the release of the decision placing punishing 29 percent protectionist tariffs on Canadian softwood lumber exports to the United States, then-Canadian Prime Minister Jean Chrétien said the tariffs put a "big question mark" over President Bush's commitment to free trade (Morton 2002). At the end of 2005, the question mark remained.

[2] In a speech on the topic of "sovereignty" to the Canadian Institute for International Affairs, then-Canadian Foreign Affairs Minister Bill Graham confirmed Canada's commitment to multilateralism, the international rule of law, and a principled approach to its place in the world (Graham 2002).

In contrast, Canada finds itself in a position similar to that which the much younger and weaker United States once occupied. As a middle power, a power-based system is one where Canada's interests will be sacrificed to a larger country's objectives. Thus, it is hardly surprising that Canada has been at the forefront of those states advocating a rules-based approach to the operation of the international economy. What is shocking is Canada's apparent recent willingness to concur in the weakening of the rules-based system by, for example, questioning the efficacy of the international tribunals created pursuant to Chapter 11 of NAFTA. Canada's principled position in international relations has sadly been weakened by its too frequent dabbling in its own version of à la carte multilateralism. How can one explain support for such a policy, which appears to cut so directly against the long-term national interest of Canada?

Canada Capitulates to U.S. Policy To Weaken NAFTA Investor Protection

It would appear that NAFTA Chapter 11 has become a flashpoint and a source of irritation for Canadian government officials in their trade and investment initiatives. Former International Trade Minister Pierre Pettigrew indicated his misgivings on the topic of NAFTA Chapter 11 (Brereton 2002). In this volume, the minister emphasized the need to balance "private interest" and "public purpose" when looking at investor protections under NAFTA Chapter 11.

The other part of the NAFTA Chapter 11 debate, and underlying the minister's rationale for stating the need for this "balance," relates to perceived threats by the investor protection provisions of Chapter 11 to Canadian sovereignty.[3] As Pettigrew noted, NAFTA

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[3] With respect to these "perceived threats" to sovereignty, the author has written specifically on this issue and the contentious question of expropriation under NAFTA Chapter 11 (Laird 2001, 223).

Chapter 11 is a "sensitive issue." The implication of the then-minister's speech is that something is broken and it needs to be fixed. However, this fixing of investor protection provisions in NAFTA may come at the cost of a trade policy built on the foundation of a rules-based system.

The government's fixing appears to have taken place at two levels: One of these is formed by the political ministers of the three NAFTA parties, and the second is made up of the Canadian courts. In the case of NAFTA Chapter 11, the United States is acting true to form — it is prepared to engage internationally until there is a perception that international rules are not meeting its interests. For the middle power countries in international affairs, such as Canada, if power politics and linkage are the only rules, that means the game is lost. NAFTA Chapter 11 provides a fundamental source of government accountability for all the NAFTA parties by relying on international law. Moreover, it ensures that government conduct is fair, principled, and non-discriminatory. While it is understandable, though regrettable, that the United States could be threatened by an international mechanism for accountability, it is incomprehensible that Canada would support such a position.

Rule of Law and Business Certainty

A commitment to the rule of law is not only a necessary survival mechanism for Canada; it is the country's longstanding foreign policy and practice. As Pierre Pettigrew says in this volume:

> Underlying Chapter 11 are basic tenets that most Canadians firmly believe in: That governments should act prudently, not precipitously, especially when it comes to the property of citizens; and that governments' decisions on the disposition of private property not be capricious, but fair, necessary and constrained by the rule of law.

In the Canadian *Statement on Implementation* of NAFTA,[4] the federal government reaffirmed its faith in Canada's reliance on the rule of law. From Canada's perspective, the object of its trade policy must be to:

> ... broaden the scope of rules-based international trade and investment and increase the opportunities for Canadian traders and investors around the world .... We must trade in order to prosper, and in order to trade we need an international trading system that is fair and open. (Canada 1994, 69, 71.)

In concluding his speech published in this volume, Pettigrew assured the audience that:

> Investment protection is thus a critical element of a rules-based trading system that has the potential to enrich those who take part. Let us all work together to build such a rules-based trading system on a worldwide level, for the benefit of all people.

The objectives set out in the text of NAFTA reflect these goals, as do the many facets of economic integration in the NAFTA area. As a comprehensive international trade and investment instrument, NAFTA is the culmination of the development of international economic law since the end of World War II.

Part of the benefit of the Canadian approach to international trade and investment is that it provides stability and predictability for business. Support for the rule of law and a certain business environment go hand in hand. There is no inherent balancing required, nor is there a contradiction. Pettigrew's position of a balancing between "private interest" and "public purpose" is a false dichotomy that creates a straw man for the Canadian government to tear down and build up again.[5] In his address, in fact, the minister appears to have adopted the anti-free traders' viewpoint on this issue, even while he disclaims their views as exaggerated.

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[4] At the time of the promulgation of NAFTA, the Government of Canada published this document to better explain the operation of the organization and the act's implementation in Canada (Canada 1994).

[5] As noted by Hart and Dymond (2002, 13) in their paper on NAFTA Chapter 11 for the Centre for Trade Policy and Law at Carleton University, "The ...

To give Pettigrew credit, however, he dismisses the view that, in the context of NAFTA Chapter 11, the private interest is trumping public purpose and agrees that the public policy debate should not be viewed in zero-sum terms. There appears to be a basic recognition on his part that it is not a question of a stark conflict of value systems, private versus public, but rather a question of making the system we share work better. In the end, however, government's actions speak louder than its words.

Pettigrew talked about a balanced approach while he was, in his apparent zeal to appease U.S. interests and Canadian anti-globalization groups, letting economic security and Canada's principled position erode. Two specific examples in the last few years help to demonstrate this. The first instance relates to Canada's regressive position on investment protections under NAFTA Chapter 11 and future trade agreements. The United States government has apparently convinced Canadian trade officials to cooperate in weakening investment protections in NAFTA, and in any future trade agreements in the Americas. The second example involves the status of international commercial arbitration in Canada and Canada's activities in our domestic courts to challenge NAFTA Chapter 11 tribunal awards. Canada had apparently reversed its decades-long support of international commercial arbitration, and the predictability it provides to business.

Canada Reverses Support for International Investment Protection

After 40 years of promoting the protection of its investments abroad, the United States appears to be reversing its policy posi-

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5 clash between state and corporation ... is neither inevitable nor necessary. While their interests are the same, they do not necessarily cancel each other out."

tion and taking Canada with it.[6] Canada pleads for the rule of law, but now appears to ignore decades of sound trade and investment policy. The government appears to have entered the world of international power politics — picking and choosing when it wants to play by international rules. Minister Pettigrew's publicly stated position in support of weaker investment protections under a future Free Trade Area of the Americas Agreement (FTAA) is a clear example of this tendency.[7]

In the post-Cold-War era, in this new age of the war on terror, the world economic and political environment is taking new forms not anticipated by the Cold War institutions. The United States has dual objectives. As the only superpower and the leader of the fight against terrorism, the U.S. needs to act multilaterally, but at the same time the administration is constrained by domestic interests and their determination to protect U.S. sovereignty, thus acting willingly in a unilateral manner where necessary.

To appease the United States, it appears that the Canadian government has decided that protection of Canadian investments abroad, and foreign investments in Canada, can be sacrificed. The problem is that, without the protections of the law such as those found in international investment instruments, many Canadian businesses may not be influential enough to defend themselves from foreign government actions that threaten their investments.

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[6] As of the end of 2003, over 2,200 bilateral investment treaties (BITs) had been signed, including over 45 by the United States, which has understandably led the way in the promotion of international investment. The debate in Congress over Trade Promotion Authority (TPA) included much discussion about narrowing and weakening foreign investor protection in the United States. The resulting recent revisions to the U.S. model in late 2004 would seem to support this conclusion. The main reason for this reversal, it would appear, was that members of Congress argued they were not prepared to allow U.S. domestic law to be subordinated to international law.

[7] Minister Pettigrew reconfirmed in the lead up to the 2001 Quebec Summit on the FTAA, his "preoccupation" with Chapter 11 and the policy position that Canada will no longer include Chapter 11-like investment protection provisions in future trade agreements, such as the FTAA (Corcoran 2001). However, it is interesting to note, that later that spring, then-Prime Minister Chrétien overruled his trade minister, apparently signalling the government's support for NAFTA Chapter 11 (MacKinnon 2001).

Irony is no stranger to international law, and the NAFTA investment chapter has been the object of much irony. By attacking investment protections and seeking to minimize the accountability of governments to the rule of law and the international law standard invoked in Chapter 11 of NAFTA, all in the name of sovereignty, the result will be in fact a loss of Canadian sovereignty. The government's attack on investment protections will lead Canada to lose the ability to make principled appeals to international rules as the basis for countering U.S. unilateralism. Moreover, the rule of law that is inherent in investment protections cuts both ways: If Canadian business wants to be protected abroad, the Canadian government has to be prepared to offer the same protections to foreign investors in Canada.

The NAFTA Free Trade Commission Chapter 11 Interpretation

On July 31, 2001, NAFTA's Free Trade Commission (FTC), a body constituted under Chapter 20 of NAFTA consisting of the three international trade ministers from the NAFTA parties, issued a *Note of Interpretation* concerning the meaning of portions of NAFTA Chapter 11 (NAFTA 2001, para. B(1)). This interpretation clearly had two objectives: (1) to deflect criticism of NAFTA Chapter 11, and (2) to narrow the playing field for Chapter 11 claimants, current and future, by limiting the substantive legal liability of the NAFTA parties.

To achieve these objectives the NAFTA parties undertook to clarify two elements of NAFTA Chapter 11: first, the provisions of the chapter related to the transparency of the arbitral process; and, second, the meaning of NAFTA Article 1105 regarding the obligation of NAFTA parties to treat investments in accordance with international law.

It can be said that the transparency element of the interpretation has had its intended affect. The more contentious element of the NAFTA FTC note relates to the narrowing of NAFTA Article

1105, which obligates the NAFTA parties to meet the international law standard of treatment with respect to foreign investments.[8]

As Pettigrew said at the time the *Note of Interpretation* was made, Canada holds that the interpretation has "reaffirmed" that the international standard in NAFTA Article 1105 "is the customary international law minimum standard of treatment" (Canada 2001). This statement is contentious because, if what the NAFTA parties say is correct, protections for investors in the NAFTA zone will be narrowed, with the potential that similar obligations in bilateral investment treaties (BITs) around the world may also be restricted.

The U.S. was seeking to narrow these obligations for a very basic reason. It was facing a number of NAFTA Chapter 11 claims based on NAFTA Article 1105, for example in the now-decided *Loewen* case decision and the on-going *Methanex* claim, and wanted to avoid losses in these outstanding international arbitrations.[9] The United States government desperately wanted to limit the scope of NAFTA Article 1105. The Canadian government had also lost two NAFTA Chapter 11 arbitrations on the grounds of a breach of NAFTA Article 1105 and also clearly wanted to limit future liability. These cases are the *S.D. Myers* and *Pope & Talbot*.

International law has a clear meaning in the practice of international law, in particular as it is set out in Article 38 of the Statute of the International Court of Justice (ICJ).[10] It is not a concept open to interpretation, or in need of interpretation. *Customary international law* is a subset concept of international law under the definition in the ICJ statute. Restricting the operation of NAFTA Article 1105 to that subset limits the effect of NAFTA Article 1105 by narrowing investor protections. The sources of international law under the ICJ statute also include treaty law, principles of international law, as well as jurisprudence. Considering that the definition of international law is not a matter that is really open to interpretation, the NAFTA Commission's interpretation of Article 1105 appears to be an attempt, in effect, to amend NAFTA by less formal means. The distinction between an interpretation and an amendment is important because the NAFTA Free Trade Commission of Ministers is not permitted to amend NAFTA, so there is a serious question as to the propriety and effect of the interpretation.[11]

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[8] NAFTA Article 1105 obligations provide: "Each party shall accord to investments of investors of another NAFTA party treatment in accordance with international law, including fair and equitable treatment and full protection and security."

[9] For a listing of the complaints referred to here, please see Table 1 in the concluding section of this volume.

[10] The Statute of the International Court of Justice is a part of the United Nations Charter and the Court is the principal judicial organ of the United Nations according to Article 92 of the UN Charter.

Pettigrew called the FTC *Note of Interpretation* an exercise in "clarification." It appears to have been an example of the NAFTA parties trying to narrow investor protections to limit the rights of all investors in the NAFTA zone. The perhaps unintended effect will be the diminution of the rights of Canadian and U.S. investors not only in the NAFTA zone, but around the world.[12]

Judicial Review of NAFTA Chapter 11 Awards in Canada

The second prong of Canada's strategy to reduce investment protections emerged, rather surprisingly, in the Canadian courts. The government aggressively challenged NAFTA Chapter 11 awards and urged an appeal-like legal review of several arbitral awards.[13] Under the terms of NAFTA Chapter 11, Article 1136, arbitral awards by NAFTA Chapter 11 tribunals may be subject to the review of domestic courts. A judicial review could permit the set-aside of arbitral awards on serious grounds, such as arbitrator misconduct, or when the arbitral decision is outside the scope of the arbitration agreement. This form of court review is not in the nature of an appeal on the law and facts.

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[11] In the damages award of the tribunal in *Pope & Talbot v Canada*, May 31, 2002, it was held that the FTC *Note of Interpretation* is an amendment, not a proper interpretation, and that the interpretive process undertaken by the NAFTA parties was not a valid exercise. See www.naftalaw.org. or www.dfait-maeci.gc.ca/tna-nac/NAFTA-en.asp2.

[12] For example, in 2004, Canada published a new model Foreign Investment Protection and Promotion Agreement (FIPA) that directly incorporates the language of the *Note of Interpretation* regarding the clause equivalent to NAFTA Article 1105. See www.dfait-maeci.gc.ca/tna-nac/documents/2004-FIPA-model-en.pdf (*Agreement*... 2004).

[13] The submissions of the Government of Canada can be found on the Department of Foreign Affairs and International Trade website at: www.dfait-maeci.gc.ca/tna-nac/NAFTA-en.asp; or at www.naftalaw.org.

Such reviews have occurred before three courts in Canada: a British Columbia court, an Ontario court and the Federal Court of Canada. In the British Columbia court, the Government of Mexico sought review of the negative decision in the NAFTA Chapter 11 case of *Metalclad*. Although the decision of the British Columbia trial court in the *Metalclad* judicial review is questionable for many reasons, it is the submissions of the Government of Canada to the court that should be the source of greatest concern to those focused on a rules-based trading system. In that review, Canada argued that Canadian courts should turn away from the weight of Canadian jurisprudence and international practice that require a high degree of deference be given to the decisions of international tribunals. Canada argued before Mr. Justice Tysoe of the British Columbia Trial Division that:

> Given the characteristics of NAFTA Chapter 11 dispute settlement, and applying the pragmatic and functional approach, it is clear that in interpreting NAFTA, Chapter 11 tribunals should not attract extensive judicial deference and should not be protected by a high standard of judicial review.[14]

In the judicial review of the *S.D. Myers* NAFTA Chapter 11 case, Canada made the same arguments to the court that it made in the *Metalclad* judicial review. In the Ontario court, Mexico again sought judicial review of the Chapter 11 award in *Feldman*. In all of these cases, Canada advocated as either party or intervenor in favour of a low standard of review of NAFTA investor-state tribunal awards, a standard that would have effectively allowed appeals of these arbitral decisions. By doing so, not only was the investor-state arbitration process undermined, but the certainty and predictability of the international commercial arbitration process in Canada was also in danger of being weakened.[15] However, none of the courts agreed with the arguments of Canada or Mexico, and each application was dismissed in its entirety.[16]

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[14] *United Mexican States v Metalclad*, Outline of Argument of Intervenor Attorney General of Canada, February 16, 2001, para. 30 (www.naftaclaims.com).

Conclusion: Feeling Power and Forgetting Right

Former Trade Minister Pierre Pettigrew suggested that a balance is required between private interest and public purpose when considering investor protections under NAFTA Chapter 11. The interests and purposes are not distinct in the manner suggested, nor should they be artificially divided. To suggest that the interests of its citizens must be balanced against the aims of government demonstrates a fundamental misunderstanding of the relation of the two as a part of a system that is integrated and symbiotic. The policy of weakening investor protections is a symptom of this misunderstanding.

The challenge for Canada is not to create conflict and carry out a false exercise of pitting the interests of the public and government against the interests of investors. As President Thomas Jefferson described the United States in 1801, the challenge for a principled middle-power is to prosper in a world of great nations who "feel power and forget right" (Jefferson 1998). This is not a zero-sum game. The private and public spheres have no choice but to work together. Canada has successfully applied this policy of international tradecraft, relying on the rule of law and the application of international law, and has prospered and succeeded. Canada forgets the international rule of law at its peril.

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[15] Two NAFTA tribunals have commented that they find Canada's position concerning deference to the NAFTA tribunals to be problematic. See *Pope & Talbot*, Ruling Concerning the Investor's Motion to Change the Place of Arbitration, March 14, 2002, para. 20; and *UPS*, Decision of the Tribunal on the Place of Arbitration, October 17, 2001, para. 11. The claims can be found at www.naftalaw.org.

[16] A summary and archive of the materials from the three judicial review proceedings are available at www.dfait-maeci.gc.ca/tna-nac/nafta_review-en.asp.

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Like a Rolling Stone:
Why a Multilateral Investment Agreement in the WTO?

John Hancock

The obituaries, it seems, were premature. Three years after the breakdown of the Organisation for Economic Cooperation and Development's (OECD) Multilateral Agreement on Investment (MAI) — and two years after the even more spectacular collapse of the 1999 trade talks in Seattle — ministers meeting in Doha in November 2001 resurrected plans for a global investment treaty in the World Trade Organization (WTO). The Doha Declaration, which spells out the mandate for the ninth round of multilateral trade negotiations, recognizes "the case for constructing a multilateral framework to secure transparent, stable and predictable conditions for long-term cross-border investment, particularly foreign direct investment (FDI)" (WTO 2001, paras. 20–22). It affirms that negotiations will take place after the next WTO Ministerial Conference, in Mexico in mid-2003, on the basis of a decision to be taken "by explicit consensus" on the modalities of negotiations. It also instructs the WTO Working Group on Trade and Investment to use the period up to Mexico to focus on clarifying a number of core issues related to a possible future multilateral framework of WTO investment rules[1] — initiating a kind of "pre-negotiation" on basic architecture before the nitty-gritty of bargaining is scheduled to begin in 2003.

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[1] These are: scope and definition; transparency; non-discrimination; modalities for pre-establishment commitments based on a General Agreement on Trade in Services (GATS)-type, positive list approach; development provisions; exceptions and balance-of-payments safeguards; and consultation and the settlement of disputes between members.

Moving to this point has not been uncontroversial. Since the establishment of an Investment Working Group at the WTO's Singapore Ministerial Conference in 1996, proponents of negotiations on investment, notably the European Union (EU), have met with stiff opposition from a number of developing countries who are sceptical about the idea of extending the multilateral trading system to cover foreign investment. Indeed sharp disagreements over investment negotiations at the WTO's 1999 Seattle Ministerial brought about one of the major causes of the meeting's collapse. Even now it is not clear that a WTO negotiation will take place. The overriding objective of ministers in Doha was to avoid another Seattle debacle — one result of which was a willingness to paper over differences with creative ambiguity in the mandate for the Round. Nowhere is this more evident than in the fuzzy language on investment — read by some as a firm agreement to negotiate, by others as an agreement merely to talk about talks. Another unknown is the future of the Round itself. Investment was – and remains — key to the balance of interests that made agreement on a Round possible. But just as progress on the larger package of issues will likely depend on progress — or lack of progress — on investment, so too will investment be held hostage to the issues that are of key interest to developing countries: agricultural subsidies, rules on antidumping, and market access for industrial products. Nothing will be agreed in Mexico until everything is agreed.

Yet behind the politics and the posturing, deeper currents are at work. With or without the formal launch of investment negotiations in Mexico, WTO members are already actively engaged in investment rulemaking across a wide front — bilaterally, regionally, multilaterally — as a logical next step towards deeper integration. There are over 2,000 bilateral investment treaties in existence today, and dozens more on the way; many bilateral and regional trade agreements now include investment chapters; and the WTO itself contains important investment-related provisions, especially in services and intellectual property. Driving this process is economic self-interest — the intense competition among countries for investment and markets, together with the growing pressure to cooperate on rules and policies across borders. The proliferation of international investment agreements is another facet of the emergence of a new rules-based global economic order — one where international economic law has become the principal instrument for managing interdependence. Like it or not, WTO members face a basic policy choice: do they continue to approach investment rulemaking in a piecemeal and fragmented way, risking a further regionalization of the international system; or do they decide to anchor investment rules more firmly in the WTO, ensuring that the system can remain relevant to this key aspect of global economic management? This may or may not be a question ministers ask themselves in Cancún. But it is central to the investment policy debate.

Bottom-Up Pressure for Top-Down Rules

The simple reason for pressure to widen and deepen global investment rules is that investment is now the main driver of global integration, and a key engine of economic growth. Recent waves of liberalization and privatization — combined with technological breakthroughs in communications and transport — has made it cheaper and easier to create dispersed and far-flung production networks, allowing multinational enterprises (MNEs) to "go global" in ways that would have been inconceivable a few years ago. Increased competition — itself a result of more open markets, and falling communications and transport costs — forces businesses to seek out new markets, acquire new technologies, achieve scale economies, reduce costs, and outsource functions that can be performed more efficiently by other economic actors. It is now commonplace for corporations to locate assembly, design, marketing, data processing, supply chains, and other activities across a range of disparate economies in order to maximize comparative advantage. Such a strategy is achieved through a variety of economic relationships ranging from greenfield investments (that is, investing in an enterprise built on a previously undeveloped site), equity holdings, and mergers and acquisitions (M&As), to strategic partnerships, licensing, and franchising. This globalization of production processes — increasingly across services as well as manufacturing — explains the surge in FDI to a peak of $1.3 trillion[2] in 2000, the fact that the sales of foreign affiliates now exceed the value of world trade in goods and services, or that well over half of trade now takes place within MNEs or with their suppliers (UN 2001).

That so many global corporations now outsource a growing share of the production process means that new opportunities to attract investment have been created for countries that were once on the periphery of the industrialized world. China, to take the obvious example, is fast becoming the world's largest destination for foreign investment — a key factor behind its rapid industrialization — after being almost irrelevant to FDI flows just two decades ago. It also means that the incentives to create a policy environment — and complementary public investment — that takes advantage of these opportunities, have dramatically increased. United Nations Conference on Trade and Development (UNCTAD) estimates that of some 1,200 investment-related policy changes worldwide since 1990, well over 95 percent have been liberalizing (UN 2001). To see the value of international investment rules in the narrow context of attracting FDI by lowering investor risk (or perceptions of risk) misses the bigger picture. Increasingly a country's international investment policy is part of a broader strategy aimed, not just at attracting capital, but at acquiring technology, skills, managerial expertise, infrastructure, and access to global networks — assets that are bundled above all in multinational corporations, the key actors in globalization. Most important of all is the link between international investment policy and domestic economic reform: the way that international negotiations provide political cover for a domestic agenda aimed at reducing barriers, strengthening markets, building institutions, enforcing laws, and encouraging transparent legal and administrative procedures — and then anchoring these reforms in external disciplines that are internationally enforceable.

At the same time, the logic of economic integration has its own dynamic. Each step towards a more globalized trade, production, and financial system has created new pressures for deeper rules and more extensive policy coordination, raising a number of important issues that require a response. How should we construct a more secure and transparent policy environment for the expansion of cross-border production? Where do we address the increasingly complex web of transfer and tax issues? What is the scope for curbing policies that distort investment flows and trade at the expense of neighbours? Is there a way to liberalize global investment without exposing countries to destabilizing financial flows? Is it possible to talk about international rules for investment without talking about international rules governing exchange rates and capital markets?[3] It is hardly surprising that the wave of foreign investment in recent decades has been matched by increasing pressure for cross-border collaboration and international agreements. These pressures are already being felt. What remains unclear is how — and in what context — governments will choose to respond.

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[2] All dollar figures in this chapter refer to U.S. dollars.

BITS and Pieces: The Rise of a New International Investment Architecture

The speed with which investment has moved on to the international agenda is reflected in the explosion of bilateral investment treaties in recent years. Although BITs have been around for decades, UNCTAD estimates that 1700 of the approximately 2000 BITs in existence today were concluded since 1990 (UN 2001). Originally negotiated between developed and developing countries, BITs now encompass a widening mix of economies — between developing countries themselves, developing countries and transition economies, and even between developed economies. BITS are also evolving into more comprehensive agreements, serving as crucibles for the development of key concepts, principles, and standards that are rapidly being incorporated in regional, plurilateral, and multilateral investment regimes.

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[3] For example, a number of countries quietly viewed WTO investment negotiations as a potential vehicle for addressing the need for rules on capital movements — and, particularly, exchange rate "safeguard" mechanisms — that they felt had arisen in the wake of the 1997/98 Asian financial crisis.

The scope of assets covered in many modern BITs is now remarkably broad — from green-field investments, to M&As, to intellectual property — and usually identified through an open, "illustrative" list.[4] General standards of treatment are also typically comprehensive. Most contain most-favoured-nation (MFN) and national treatment requirements (although a significant number specify only MFN treatment), and commonly require that investments be accorded fair and equitable treatment, full protection and security, and that the parties refrain from impairing the "management, maintenance, use, enjoyment or disposal of covered investments" by unreasonable or discriminatory measures. Virtually all BITs contain obligations related to the transfer of funds flowing from investments, expropriation, and compensation, and protection from losses due to war and other extraordinary circumstances. Treaties concluded by the United States often also deal with performance requirements, temporary entry of certain personnel, and the right of foreign investors to hire top management without regard to nationality. Finally, many BITs provide for binding international "investor-state" arbitration — the significance of which is now increasingly being tested.[5]

At the same time, there has been a proliferation of regional investment arrangements in an effort to catch up to market-driven integration, and to coordinate investment policy over wider geographic areas than can be achieved in BITs. The significant feature of most regional agreements — and now a growing list of bilateral trade agreements — is that they deal with investment as part of broader economic integration arrangement centred on trade. The

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[4] These illustrative lists typically include moveable and immoveable property, ownership rights in companies, claims to money, and intellectual property rights.

[5] Arbitration of intergovernmental disputes is regulated by specific rules laid down in each BIT concerning such matters as the method of appointing the arbitrators, rules of procedure, the time limits for the completion of the arbitration proceedings, liability for costs and applicable law. In addition, there often are provisions for binding international arbitration of disputes between one of the parties and a national of another party. Such provisions normally refer to pre-existing arbitration rules, notably those under the International Centre for Settlement of Investment Disputes (ICSID) Convention.

North American Free Trade Agreement (NAFTA), for example, is as much an investment agreements as a trade agreement, insofar as the creation of an integrated market has proven to be a powerful magnet for FDI.[6] Regional investment agreements vary widely in terms of form, scope, depth, and process. Some are much less ambitious than most BITs. The Asia Pacific Economic Cooperation (APEC) forum's Non-Binding Investment Principles, for instance, deal with transparency, non-discrimination between source economies, national treatment, investment incentives, performance requirements, expropriation and compensation, repatriation and convertibility, settlement of disputes, entry of personnel, avoidance of double taxation, and the removal of barriers to capital exports. Apart from the fact that these principles are not legally binding, in most instances their formulation is considerably less specific and stringent that in many other investment treaties. Other arrangements essentially "regionalize" existing BITs. A case in point is the 1987 agreement among the Association of Southeast Asian Nations' (ASEAN) members for the Promotion and Protection Investments. It merely provides that the parties shall encourage foreign investment from other parties, but subject to their domestic laws and objectives. Moreover, national treatment after admission is not a general obligation but a matter for negotiation between the parties to the agreement. An example of a more ambitious variation of the bilateral model — a "BIT-plus" — is the 1994 Colonia Protocol on Promotion and Reciprocal Protection of Investments within the Mercado Commun del Sur (MERCOSUR, the South American common market). It requires parties to accord the better of national treatment or MFN treatment in regard to both the admission of foreign investment from other parties and the treatment of such investment after admission. During a transition period, this obligation is qualified by the right of each party to maintain exceptions in sectors listed in the annex to the protocol.

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[6] A case in point is Mexico which has seen FDI inflows generally rise since the early 1990s — against declining trends across much of Latin America — in part because it provides a platform to access NAFTA's market of 360 million people.

The investment provisions in NAFTA are also comparable to BITs — but with some important additions. Like the BITs, the provisions of Chapter 11 include a wide definition of the term investment, general standards of treatment (including national treatment, MFN, and treatment in accordance with international law), specific standards for compensation in the case of expropriation and other losses, transfers, and a mechanism for arbitration of disputes between an investor and a party to NAFTA. In important respects, however, NAFTA's investment disciplines go far beyond those contained in a typical BIT. For instance, the requirements to accord national treatment and MFN apply both to the admission of investments and the treatment of investments and investors after admission. NAFTA's scope of prohibitions of performance requirements is also unprecedented in international investment or trade agreements. Other unique features of NAFTA are the inclusion of rules on environmental matters and the provision for consolidation of state-to-investor arbitration proceedings in case of multiple claims involving common questions of law.

Then there is the European Community Treaty — easily the most far-reaching approach to the regional integration of investment laws and policies. It envisages the removal of restrictions on the right of establishment and movement of capital, a principal means of establishing a single market, something which distinguishes it from all other arrangements in the field of foreign investment.[7] Articles 52–58 of the EC Treaty provide for the progressive elimination of restrictions on the freedom of establishment of natural and legal persons that have the nationality of one member state in the territory of another — the so called "single passport" approach of rights of establishment. Articles 67–73 address the progressive elimination of restrictions on the free movement of capital. Taken together these provisions create the closest thing yet to a single pan-regional investment regime. Moreover, these same measures are also addressed in agreements the EU has reached with third countries, including its association agreements with countries in Central and Eastern Europe.

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[7] Even where, as in the case of the investment provisions of NAFTA and the BITs concluded by the United States with third countries, the entry of foreign investment is subject to binding national treatment and MFN treatment requirements, the scope of such obligations is less far-reaching than the requirements of the EC Treaty regarding the right of establishment and free movement of people.

Half Pregnant: WTO's Partial Embrace of Investment Rulemaking[8]

Pressure to address investment issues is also being felt in the WTO itself. When the General Agreement on Tariffs and Trade (GATT) came into force in 1948, little in its rules related directly to investment. But as the system has evolved through successive rounds of negotiations, and, in particular, through its transformation into the WTO, investment-related issues have moved to the forefront of the agenda. One reason is that the system's rules have progressively come to focus on domestic policy instruments that can affect trade — like subsidies, technical standards, and government procurement. Although rules in these areas were designed to address trade distortions, many are also relevant to investment. A more significant reason why the WTO system is now grappling with investment issues is the growing realization that the scope for increased trade — and market access — hinges on the scope for companies to operate in foreign markets; a reality already reflected in key provisions of the Services Agreement. So while investment has found its way into the WTO system almost by accident, or as an after-thought, typically in response to specific trade policy problems, the cumulative result is a set of rules and obligations under the WTO umbrella that pertains directly or indirectly to foreign investment (WTO 1996, 69–73).

The General Agreement on Trade in Services (GATS) is the clearest example of how far investment issues have moved into the mainstream of the WTO. Once members had agreed to tackle services liberalization in the Uruguay Round, it became clear that it was difficult, if not impossible, to supply many services to a market without the physical presence of the service supplier — that is, without foreign investment. Thus, Article I of GATS defines trade in services in terms of four modes of supply, including the supply "by a service supplier of one member, through commercial presence in the territory of any other member."[9] It is true that GATS is not an investment agreement in the same sense as most international investment agreements; its focus is on the ability to supply a service rather than on investment per se, and one of its essential features is that the establishment of a commercial presence in a host country be "for the purpose of supplying a service." While the concept of commercial presence provides for rights of entry or market access (pre-establishment treatment), it does not provide for the rules on the treatment or protection of foreign investment once established in a market (post-establishment treatment) — e.g., in such areas as expropriation and compensation. The obligations of GATS also differ in respect to their general applicability. Certain obligations, such as MFN treatment, are in principle applicable to all members and all service sectors, whereas obligations relating to market access and national treatment apply only to specific commitments made by members in their schedules of commitments.[10] Plus, obviously, the GATS provisions only relate to investments in service industries; no equivalent GATT provisions govern "commercial presence" in the resource or manufacturing sectors.

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[8] This section is based on Mark Koulen's detailed discussion of WTO investment-related provisions (Koulen 2001).

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[9] The term *commercial presence* is defined in Article XXVIII(d) of GATS as "any type of business or professional establishment, including through (i) the constitution, acquisition or maintenance of a juridical person, or (ii) the creation or maintenance of a branch or a representative office, within the territory of a member for the purpose of supplying a service." Another investment-related mode of supply covered by Article I:2 is the supply "by a service supplier of one member, through presence of natural persons of a member in the territory of any other member." This mode of supply is closely related to commercial presence in that it includes temporary entry of business visitors and intra-company transfers of managerial and other key personnel.

[10] Specific commitments regarding market access and national treatment apply only to service sectors listed in these schedules and are subject to conditions and qualifications specified therein. With respect to market access and national treatment, GATS involves a combination of a positive list approach to the identification of the specific sectors that are covered by a member's commitments with a negative list approach to limitations on market access and national treatment in those sectors.

If GATS addresses market access issues but not protection, the Trade-Related Intellectual Property (TRIPS) agreement does the reverse. It essentially lays down minimum standards of substantive protection for intellectual property — brands, trademarks, patents, copyrights and so forth which, when they cross borders, are clearly forms of *foreign investment*. These standards must be available in the national law of each member, requiring that the substantive obligations of the main international intellectual property agreements — for example, the World Intellectual Property Organization (WIPO) Conventions, the Paris Convention, and the Berne Convention — be complied with, and by adding a number of additional obligations in areas where existing conventions are weak or silent. The TRIPS agreement also sets out, for the first time in international law, the procedures and remedies that each member must provide within its national laws so that the nationals of other members can effectively enforce their intellectual property rights — whether through the normal civil or criminal judicial process, or through customs action against imports of counterfeit or pirated goods. So while the TRIPS agreement does not address investment directly, its provisions on minimum standards for the protection of intellectual property, domestic enforcement procedures, and international dispute settlement are directly relevant to the legal environment affecting foreign investment — as underscored by the fact that many international investment agreements included intellectual property under their definition of investment. What the TRIPS agreement does not do is set out wider obligations governing the entry and protection of foreign investment as such. And of course the agreement covers only one category of foreign investment — intellectual property — leaving all other assets outside the ambit of WTO rules.

Then there is the Trade-Related Investment Measures (TRIMs) agreement that focuses on performance requirements, but only to the extent that such measures discriminate against trade in goods. First it clarifies that certain types of investment measures are inconsistent with GATT Articles III (national treatment) or XI (quantitative restrictions); second it requires that all inconsistent

TRIMs be eliminated within a certain period of time (two years in the case of developed countries, five years for developing countries, and seven years for least-developed countries — although several extensions have recently been granted); and third, it provides for a five-year review of the agreement, (at which point consideration was to be given to whether it should be complemented with provisions on investment and competition policy). The trade-oriented nature of the TRIMs agreement means that its obligations are much narrower in reach than the disciplines on performance requirements found in some existing investment agreements, such as NAFTA.[11] Another limiting feature of the TRIMs agreement is that it applies only to trade in goods, not to trade in services. Finally the agreement does not attempt a generic definition of trade-related investment measures, but relies instead on its annexed illustrative list — leading to growing debate over how "illustrative" the list is (or ought to be) and whether there is any scope to expand its coverage.

Finally the Subsides and Countervailing Measures Agreement (SCMA) is also relevant to investment, in that its provisions can potentially impact on investment incentives — and indeed two cases, Indonesia-National Car and Canada-Aircraft, have had prohibited subsidies' challenges to investment incentives (although not focused on incentives for foreign inward investment). Financial incentives (such as the direct provision by a government of funds through grants and subsidized credits) and fiscal incentives (such as tax credits) would generally fall under the definition of a subsidy, as outlined in Article 1. So, too, would certain kinds of indirect investment incentives (for example, the provision of land and infrastructure at less than commercial prices). To the extent that investment incentives are specific to certain enterprises or industries, within the meaning of Article 2, they are subject to the substantive disciplines of the agreement. Nevertheless, the agreement's disciplines are focused on the adverse effects of subsidies for trade — not subsidies for investment per se — thus limiting its potential applicability to investment incentives.[12]

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[11] Technology transfer requirements, for example, are not covered by the TRIMs agreement since these measures are not inconsistent with GATT (WTO 2002, paras. 26-69).

The point is that most of the key concepts found in international investment agreements — market access, protection, incentives, and dispute settlement — are already embodied in one WTO agreement or another, but in a disjointed, ad hoc way, reflecting the evolution of the system in response to specific trade-related issues or problems. The debate about bringing investment into the WTO is therefore a false debate. Investment is already in the WTO. The question facing members is what to do with it?

What Is At Stake?

Investment is at the epicentre of global economic relations. It touches on — and crosses over into — issues related to trade, capital flows, macroeconomic policy, technology transfers, domestic regulation, and the complex interface between private and public interests. It is becoming impossible to talk about the management of globalization without talking about global rules for regulating investment and capital flows. Nothing is more "globalized." Yet the defining characteristic of today's international investment architecture is its "un-global" nature. Too many countries — especially in the developing world — are outside the system altogether.[13] Others are simultaneously parties to multiple and overlapping agreements — bilateral, regional, or plurilateral. And these agreements themselves are hugely diverse — binding and non-binding, with and without commitments on admission, with and without provisions on corporate behaviour, with top-down and bottom-up architectures, part of broader trade agreements or standing outside.

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[12] Since investment incentives are usually granted in advance of production and trade, provisions of the agreement would require an after-the-fact assessment of adverse trade effects of such incentives (Koulen 2001).

[13] A major concern is the widening gap between an industrialized world increasingly linked together by foreign investment and large parts of the developing world that remain on the periphery. UNCTAD reminds us that the world's top 30 host countries account for 95 percent of investment stocks. The top 30 home countries account for around 99 percent of outward FDI flows and stocks, mainly industrialized economies. About 90 of the world's largest 100 non-financial TNCs [Transnational Corporations] in terms of foreign assets are headquartered in the Triad" (UN 2003, xv). Developing ...

The arguments for multilateralism in trade relations apply equally for investment relations. The multilateral system gives even the smallest and poorest countries greater leverage and security than they would otherwise have outside the system. It allows countries to pool their interests and build coalitions — in contrast to bilateral negotiations where smaller countries have virtually no clout negotiating one-on-one with the great powers. It also creates more scope for trade-offs involving a larger number of countries, which in turn create more balanced and comprehensive outcomes. And the multilateral system is non-discriminatory (rooted in the core principles of national and MFN treatment) — whereas bilateral or regional deals by definition exclude and marginalize non-participants. In fact, the logic of bilateralism lies precisely in discrimination and power asymmetries — the ability of larger economies to impose conditions on weaker ones, and to use preferential rules and regulations to "capture" and divert investment flows (which may partly explain bilateralism's curious appeal to certain host, as well as home, countries). The very fact that the United States is lukewarm towards a WTO agreement — because of concerns about "free riders" and the risk of diluting its aggressive bilateral agenda — is precisely why developing countries, concerned about leverage and flexibility, should be first in line to embrace the multilateral option. Bringing developing countries into a system of multilateral investment rules would not solve their FDI difficulties overnight. Rules, by themselves, do not create investment flows; that is up to private sector. What a multilateral

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footnote 13 continued

... countries are not just missing out on the current wave of foreign investment, but on the bundle of direct and indirect assets which accompany it — access to technology, managerial know-how, and the global distribution and trade networks that TNCs now embody. Indeed, because of the growing volumes of intra-firm trade, developing countries that fail to integrate into this FDI-driven system of globalized production risk being relegated to a second tier of international trade — essentially the suppliers of raw materials and low-tech manufactures.

agreement would create is greater "equality of opportunity," a levelling of the international playing field.

A related concern is the growing fragmentation of investment regimes — and the risks this carries for a further weakening and fracturing of the global economic system. In an ideal world, regional and multilateral approaches would interact in a positive and mutually reinforcing way as, in some respects, they have done. The removal of investment barriers regionally has generally made economies more competitive, and less resistive to the idea of global liberalization. Regional approaches have also been crucibles for policy innovation, the results of which have frequently spilled over into the multilateral arena — witness how NAFTA's work on services and intellectual property found its way into the Uruguay Round and its results. But while bilateral, regional and multilateral agreements can complement one another, they can also result in overlaps, inconsistencies, and gaps that compromise the clarity of the system, and make it difficult to navigate through a tangled web of rules — not just for investors, but for countries with insufficient human and institutional capacity to manage increasingly complex and dense international regimes. The bigger danger arises when regionalism becomes a substitute for multilateralism — or worse when it serves as an instrument for carving out preferential access to key global markets. In a world where investment is key, not just to capital flows, but to flows of production, technology, and trade, regional arrangements that are discriminatory — in terms of rights of establishment, licensing requirements, certification, regulations, and standards, and the movement of people — can give rise to conflict and impact negatively on global economic stability. This is especially true when these arrangements are as far-reaching as, say, the proposed agreement for a Free Trade Area of the Americas (FTAA) or APEC.

This raises even larger concerns about the continued relevance of the WTO. Investment has found its way into the WTO system almost by accident, or as an after-thought, usually in response to specific trade policy problems. But in a world of increasingly complex economic and financial relations, where the boundaries between trade and investment, services and manufacturing, "hardware" and "software" are becoming more and more blurred, many of the WTO's existing investment-related measures risk seeming incomplete, if not irrelevant. Can there be comprehensive trade liberalization without comprehensive investment liberalization — when over half of world trade now takes place within multinational corporations? Why set out investment rights for services but not for manufacturing — when it is becoming impossible to describe a General Motors or IBM as a manufacturer or a service supplier? Does it make sense to discipline trade distorting subsidies but not investment distorting subsidies — when the two are practically indistinguishable? And can we talk about rules on foreign investment without talking about broader rules on capital flows — when modern financial instruments are rapidly leaving behind quaint categorizations like FDI or portfolio investment? Everywhere one looks — bilaterally, regionally, plurilaterally — investment rules are the subject of negotiations; everywhere, that is, but in the WTO. Without a comprehensive negotiating mandate on investment, WTO rules will start losing their efficacy and legitimacy. The risk is that the multilateral system will gradually be bypassed by regional agreements that are viewed as more relevant to the transformational changes underway in the real economy.

Rules matter. There is a temptation — at a time when markets, not governments, occupy the "commanding heights" — to assume that international economic policy can be "privatized," and that transnational corporations, bond traders, and investment bankers now write the rules of the game. This is a dangerous fiction. Globalization did not just happen. It is the result of conscious policy decisions by governments, not only to liberalize their markets, but also to cooperate across borders on the basis of international agreed rules and procedures. Markets — including global markets — only work as well as the policies, regulations, and laws underpinning them. And if international rules are essential to the security and predictability of world trade, they are that much more important to international investment flows, where the economic stakes can be far larger (literally billions of dollars in recent mergers), and where transactions are measured in years and decades, rather than days and weeks. As economic integration deepens and our interdependence increases, the rules and procedures of the WTO provide a kind of "global economic constitution" — undergirding increasingly integrated markets, and helping governments work out ways to achieve their policy objectives cooperatively.

The question is not *whether* countries want international investment rules — the proliferation of agreements shows that the majority do — but *how* and in *what* context. Will they continue to pursue bilateral and regional approaches — in inherently unequal and unbalanced negotiations — or attempt to consolidate their interests in a multilateral effort? Will international investment rules remain preferential and fragmented, risking beggar-thy-neighbour policies, and a further regionalization of the global economic system? Or will they be defined by the non-discriminatory principles of the multilateral system? While governments may not like the idea of new WTO rules, or of tackling the difficult policy and political challenges involved in comprehensive investment negotiations, especially after the bruising Uruguay Round experience, they should be even less enthusiastic about finding themselves on the receiving end of the new bilateral or regional investment architecture that is taking shape around them. A few years down the road, it may turn out that the only thing worse than being part of a WTO investment agreement, is not being part of a WTO investment agreement.

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Prologue to *Like a Rolling Stone: Why a Multilateral Investment Agreement in the WTO?*

John Hancock

If there is a lesson to be drawn from my chapter, "Like a Rolling Stone: Why a Multilateral Investment Agreement in the WTO?", it is the folly of trying to predict the outcome of World Trade Organization (WTO) negotiations. When this paper was first drafted in 2002, the prospects for bringing investment rules into the WTO looked cautiously good. Trade ministers had agreed to include investment in the newly launched Doha Round (subject to reaching consensus on the scope and timing of the negotiations before their next ministerial meeting in Cancún), the Investment Working Group had been mandated to clarify core elements of a prospective agreement, and the secretariat had embarked on an ambitious program of investment-related technical assistance around the world. In 2005, the picture is very different. The failure of the Cancún Ministerial Conference in September 2003 effectively killed any hope of including investment negotiations in the "single undertaking" of the Doha Round — a reality confirmed ten months later with the General Council's decision to drop investment (along with two other "Singapore Issues") from the Doha agenda.[1]

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[1] The July Framework Agreement (WTO 2004), which reconfigures — and reduces the ambition of — the Doha Round, states that investment (together with competition policy and transparency in government procurement) "will not form part of the Work Programme set out in that Declaration and therefore no work towards negotiations on any of these issues will take place in the WTO during the Doha Round." The language not only appears to explicitly exclude the possibility of any negotiations on investment — including plurilateral approaches — for the duration of the Doha Round, however long ...

Although further analytical work on investment can in theory continue — and the working group remains intact — the likelihood of reaching an investment agreement in the WTO is probably nil for the foreseeable future.

On the one hand, the bleak prospects for an investment agreement disappointed those who believed that investment belongs alongside trade in the WTO, and for whom investment negotiations were an important part of the political balance struck when the round was launched. On the other hand, it was seen as a minor victory by those who either felt unprepared for full-scale investment negotiations, or who had never been convinced of the rationale for a multilateral investment agreement in the first place. It did not, however, come as a complete surprise to anyone. After all investment has a long history of controversy in the multilateral trading system. Disagreements over proposed investment provisions helped to kill the idea of an International Trade Organisation (ITO) back in the late 1940s, forcing countries to fall back on the previously negotiated commitments for what became the General Agreement on Tariffs and Trade (GATT). Another effort to tackle investment in 1955 — in the form of a GATT resolution urging the negotiation of bilateral and multilateral investment rules — failed to materialize for similar reasons. Again, in the early 1980s, several countries pushed unsuccessfully to have investment included in the package of issues to be negotiated in the Uruguay Round; although the final agreement included a number of important investment-related provisions, there was no agreement to negotiate a separate legal instrument on investment. This was followed by the breakdown of the Organisation for Economic Co-operation and Development's (OECD) Multilateral Investment Agreement

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footnote 1 cont'd.

... that takes, but it also raises questions about what — if anything — the working groups can constructively do now that they are prevented from doing any work that might lead towards eventual negotiations. The exception is trade facilitation, the one "Singapore Issue" on which members have agreed to negotiate. Arising from the 1996 Singapore Ministerial, the "Singapore Issues" are investment, competition, government procurement, and trade facilitation (i.e., cutting red tape).

(MAI) negotiations in 1998, and the even more spectacular collapse of efforts to launch a new round — including investment negotiations — at the WTO's Seattle Ministerial Conference in 1999. Investment has been — and, I believe, will remain — among the most sensitive and heated issues facing the WTO.

Just as it proved premature to assume success for investment negotiations after Doha, it would have been equally premature to assume failure. For 18 months after the launch of the Round in November 2001, good progress was made in the WTO at the technical level clarifying and then re-clarifying possible elements of an eventual investment agreement — to the point where on all core issues the position of most members was well understood[2] — although the key issue of launching negotiations was avoided until shortly before the Cancún Ministerial. If negotiations on other parts of the round, particularly agriculture, had advanced satisfactorily by that time, it might have been possible to move to the stage of agreeing to modalities for investment negotiations. In the absence of progress on market access and a solution to the problem of cotton in Cancún, however, pressing the case to start investment negotiations only helped precipitate crisis. In a last minute bid to salvage the talks, European Union (EU) Trade Commissioner Pascal Lamy offered to drop the EU's long-standing demand for launching investment negotiations in return for tacit agreement that the rest of the Cancún package — especially a possible compromise on agriculture — would survive. When Cancún failed anyway, the EU tried in the following months to put investment back on the negotiating table, but it was too late. No one believed any longer that investment was a make or break issue for the EU (or indeed any of the other proponents); Humpty Dumpty could not be put back together again.

This leaves a curious contradiction: Even as the WTO abandons plans for a multilateral investment agreement — at least for the current Doha Round — the number of bilateral and regional agreements is exploding fuelled by the worldwide scramble to attract foreign direct investment (FDI). Certainly the belief that dropping investment from the WTO somehow will make the issue disappear from the international agenda seems misguided. It only means that countries have lost (at least temporarily) the multilateral option for dealing with the unavoidable policy issues arising from the globalization of investment — leaving them to be addressed bilaterally (where demands will be higher, and leverage will be weaker), or in dispute settlement (where panels, not governments, will decide). It also means that the WTO has been weakened. The fact that progress on almost all new issues (competition policy, transparency in government procurement, regionalism, as well as investment) is now blocked is a setback for WTO rulemaking. It reversed an expansionary trend that began with the Kennedy Round, and reached its peak with the Uruguay Round, raising fresh doubts about the WTO's future relevance to a fast-changing global economy, and giving new impetus, and rationale, to the proliferation of bilateral and regional deals. For countries, especially in the developing world, that depend on the rules of the multilateral system to counterbalance the leverage of the great economic powers, the collapse of investment talks paradoxically reduces, rather than expands, their options.

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[2] That is, the scope of a possible agreement, substantive provisions, how specific commitments might be scheduled, and dispute settlement.

In a broad sense, then, the article's core argument remains as valid today as it was two-and-a-half years ago: There is a wide consensus about investment's role as a key driver of global economic growth, as well as integration. There is a clear case for global rules to help consolidate the tangled web of bilateral and regional deals already in place, to multilateralize their commonalities, and to make a start towards filling in gaps or inconsistencies between them. And there is a compelling argument for anchoring a multilateral agreement in the WTO, not just to avoid conflict with its existing investment-related provisions, but for wider systemic reasons — that is, the breadth of the WTO's membership, the scope of its rules, and the efficacy of its dispute settlement system. Indeed, if a global investment agreement cannot not find a home in the WTO, it is difficult to see where else it can go — precisely the argument that many WTO members made after the failure of the OECD's own MAI efforts in the late 1990s.

The issue facing WTO members is not so much whether they are prepared to bind their investment policies under international rules — the proliferation of bilateral investment treaties shows clearly that the majority of them are — but whether they prefer to continue to forge those agreements bilaterally and regionally, or to consolidate a large part of the exercise under a single multilateral investment agreement to be administered by the WTO. The 2,300 plus bilateral treaties in existence today are, by their nature, preferential and discriminatory, in some cases marginalizing and damaging third-country interests. They raise obvious concerns about the cost involved in negotiating and administering them (over 10,000 bilateral treaties would be needed for all WTO members to be accommodated in this way), and their potential for legal inconsistency. Last but not least, they place developing countries in an inherently weaker position. Pooling influence and interests in a multilateral context should be a much more attractive proposition for developing countries than negotiating one-on-one with their major economic partners.

Will there be a renewed push to bring investment into the WTO? Will the rationale be clearer and more compelling? Will other models be explored — such as voluntary or plurilateral approaches? And will developing countries be more amenable to the idea of multilateral investment rules, as their economies continue to grow, their interests diversify, and investment flows become even more central to global economic integration? I predict that the decision to drop investment from the current Doha Round does not signal the issue's "obituary." It is a setback for the WTO, certainly, but far from the end of this very long story of multilateral investment.

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A Commentary on "Like a Rolling Stone"

Louis W. Pauly

John Hancock has given us an excellent *tour d'horizon* of the new landscape facing trade negotiators as they contemplate a more assertive move to set rules for international investment. His chapter is particularly good at sketching the historical background that connects bilateral investment treaties to the kinds of multilateral investment agreements now being negotiated in regional and global contexts. The underlying logic of the chapter, the logic of liberal inevitability, is impeccable, at least by its own lights. With pride of place given to market forces, the central argument is itself driven forward, like a rolling stone.

I agree with most of Hancock's views. The continued rationalization of an integrating world economy certainly seems necessary. In this regard, the proposition that trade issues can no longer easily be separated from investment issues is now widely accepted — in principle, if not yet always in practice. That principle itself, moreover, now justifiably occupies a prominent place among the constellation of issues that concern the few hundred professionals comprising the headquarters staff of the World Trade Organization (WTO) in Geneva. For present purposes, nevertheless, it seems worth probing the extent to which they and we should rely on the logic of inevitability if global rulemaking on the trade-investment linkage is to succeed. Is there an alternative perspective that might help us see more clearly the impediments that might — in practice if not in principle — stop that rolling stone?

In the early 1980s, I went to Ottawa to interview a senior mandarin on the subject of Canada's investment regime in the financial sector. What he told me certainly stuck in my memory. I had confidently described a world where the right-of-establishment, the obligation of states to accept at least certain types of inward investment from business firms based in like-minded states, was now evolving into a global regime. What, I asked, did he think of it? Surely he agreed that such a regime was inexorably being constructed. To my surprise, he disagreed. "Look," he said, "that's an American idea, and an idea for a world dreamed up by Americans. We do not use that phrase here. There is no right of establishment, certainly not in financial services, which comprise the commanding heights of our national economy. In this regard, there is only a privilege of establishment, and only the sovereign Government of Canada can grant that privilege" (Pauly 1988, ch. 5).

That response almost seems quaint now. Certainly that's what a hard-core liberal perspective implies. If global companies, operating in global markets, will sooner or later get the kinds of rules necessary to reduce uncertainty and summon up the confidence to invest widely and for the long term, then a system of specified rights and responsibilities will have to replace contemporary *ad hoc* arrangements at the global level, where privileges granted can easily and without recourse be taken away. Indeed, sooner rather than later appears certainly to apply to the economic relationship between Canada and the United States. Succeeding the Canada-U.S. Free Trade Agreement, the North American Free Trade Agreement (NAFTA) embodies a new set of rules designed to apply across a wide range of activities. The language of rights is commonly used to explore the implications of those rules, although it remains noteworthy that significant restrictions and reservations remain in certain key sectors. Moreover, there are now systematic procedures for dispute settlement and judicial limits on the kind of executive caprice so obvious in an earlier era, when decisions to invest depended simply on the granting of a privilege, and when that very idea of privilege-granting reached operational status — both in Canada and the United States — in official procedures for reviewing foreign investments to ensure their conformity with the national interest. Something has quite evidently changed since my long-ago interview in Ottawa.

A few years ago, I was in Taiwan, interviewing senior executives in the semiconductor industry. I was startled at one point to hear a response along the following lines from one of those executives, who after all is based in what we in Canada still call an emerging economy. He noted, "We are currently looking at a potential greenfield (new) foundry site near someplace called Brampton, Ontario. We may build there. Good transportation systems close to our main customers, very good universities nearby, subsidized health care for our workers, lots of cheap skilled labour — cheaper than in Taiwan even after accounting for the fact that Taiwanese workers are more productive — and a welcoming government, which certainly seems to want us there very badly" (Keller and Pauly 2000, 327–352). Who was granting privileges now?

On its surface, this latter interview certainly seems to support Hancock's argument. Market forces appear to be in the driver's seat, with governments mainly playing the role of supplicant. They need the investment, and they need it badly. If foreign investors want investment agreements to make them more comfortable, then they will get them. But is there more here than meets the eye?

How well founded is the notion that what we are witnessing in the international investment arena are governments in retreat from the inexorable force of the market? How acquiescent should analysts and observers depict them to be? Could it be that the Canadian case is suggestive, not of inevitable resignation to external developments, but of aggressive and intentional action to change the tone and trend of internal economic governance? Could it be that, as a matter of national strategy, Canadian policymakers have not reluctantly fallen into line, but instead decided to join enthusiastically in the heightening interstate competition for jobs, for capital, for the maximum feasible degree of autonomy in a changing international system, and for the continuing security of Canada's place among the principal powers within that system? Similarly, could the decision not to include investment in the Doha Development Round signal political resistance to "inevitable" market forces among certain states outside that privileged group?

This kind of language, the language of political realism, may itself strike most readers of this volume as anachronistic. The language of economic liberalism — with its ineluctable and still-hopeful conclusion — is certainly more comforting. Even most anti-globalizers seem to be comforted by its logic. Few — and none whom I personally know — really seem to want to turn the clock back to closed markets and self-reliance. Instead, they seem to want the outcomes of modern capitalism to be cleaner, more sustainable, and certainly more just. But what if there is nothing necessarily liberal about the act of opening up national markets and of accepting the spread of foreign investment, either at the level of intention or the level of immediate consequence? What if, at best, durable openness, interdependent prosperity, and sustainable development follow only in the long run in a system that manages reliably to channel an enduring interstate struggle for power away from the military arena to the economic one? If the alternative language of realism can be used, even if only tentatively and for the sake of the present discussion, then perhaps it can open our minds to the conditions that gave rise to such a system. Perhaps it can also usefully caution us against assuming that the system is now on auto-pilot.

In any event, it seems to me quite plausible to argue that a struggle for power and position still energizes a world mainly organized around states. The post-World War II opening of certain national markets may have been a successful strategic tool used to underpin a new global governing coalition and ultimately to defeat the surviving challenger. In the wake of the Cold War, the expansion of trade and investment opportunities, the stabilization of financial markets (which support that expansion when they work well or threaten it when they go awry), may continue to be directly linked to a larger strategy still aimed primarily at global political stability. Proponents may call such an outcome peace. Doubters may see it more in terms of avaricious exploitation that sows the seeds for the next great transformation in world politics. Be that as it may, my point is that if a more realistic way of thinking retains a degree of plausibility, it necessarily undercuts the logic of inevitability that economic liberals bring with them to discussions of such seemingly mundane matters as investment rules. It suggests instead, for example, that such rules are the voluntary price that other states must pay if they want to export goods and services into the U.S. market. It suggests that they may have to grant protection for some types of intellectual property if they want to benefit from investment inflows. It suggests that they will be under pressure to trade access privileges in their financial sectors for market openings elsewhere. It suggests acquiescence in rulemaking by the strong in the full knowledge that the strong will not always be ruletakers. It suggests, in short, that we remain in a world of contingency, of political struggle, of the perennial contest between human wisdom and human imprudence — and not in a world of inevitable progress toward greater rationality.

In such a light, trade and investment agreements between Canada and the United States may be of limited assistance in helping us discern the direction of policy change at the global level. It could be, for example, that at a turbulent moment in world economic history and a vulnerable moment in its own national experience, Canada requested and then acceded to a free trade agreement with the United States designed to give it a better shield against any movements toward market closure abroad or in the United States itself. A few years later, it could be that Canadians engaged in the NAFTA negotiations mainly to defend the gains accruing from that earlier agreement.[1] It could also be that Mexico, and Canada to some extent, came to see the final NAFTA agreement not so much as necessary to accommodate external pressures, but precisely in order to facilitate and promote an internally generated program of domestic reform.[2]

While such examples do not suggest the inevitability of global rules for global companies, in a more realistic framework of analysis they can remind observers and policymakers to look for moments when new rules might be negotiated, and perhaps codified, in other contexts. The ill-fated Multilateral Agreement on Investment, promoted quite aggressively in the late 1990s by the Organisation for Economic Co-operation and Development

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[1] For an articulation of this basic point, see Cameron and Tomlin (2000, 63-64).

[2] Cameron and Tomlin (2000, 125) make this argument quite convincingly as well.

(OECD), obviously did not coincide with such a moment. A similar conclusion seems justified with regard to multilateral investment rules in the WTO, at least during the latest round of trade negotiations.

Antiglobalizers claim credit for killing investment protections in the OECD through global social mobilization. If political realists are closer to the mark, however, it could be that new investment rules at the global level are only feasible when broader forms of reciprocity are available, say when market access for certain imports can be exchanged for guarantees regarding the treatment of foreign investors and their intellectual property, or when idiosyncratic domestic political agendas happily coincide. Such musings, of course, bring us straight back to John Hancock's WTO, where such large-scale and reciprocal trade offs are feasible. They bring us back there, nonetheless, with a deeper appreciation of the intrinsically political challenges ahead. They remind us, too, that bringing the investment agenda more fully into the WTO may be the means to an end, not the inevitable end itself.

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Conclusion — Investor Protection in the NAFTA and Beyond:

Private Interest and Public Purpose

Alan S. Alexandroff

The authors and their chapters in this book chronicle what in another context was described as a, "sexed-up dossier." Investment and investment protection provisions are significant and today raise contentious discussions over public policy. Investor protection, principally through the North American Free Trade Agreement (NAFTA), Chapter 11 is the stuff of "above-the-fold" newspaper reading in Canada and increasingly so in the other two NAFTA countries, as well. And this debate is loud. The Canadian parliamentary committee examining NAFTA in late 2002 acknowledged the public emotion over investor protection in NAFTA:

> The issue is simply one of policy: how to balance investment protection, including the corollary rights of private investors, with public control over governmental policymaking. The mere fact that Chapter 11 has generated so much widespread commentary — whether based on deep analysis or pure emotion — indicates that something is seriously wrong with the status quo and signals pressing unfinished business within the NAFTA framework. Our hearings emphatically confirmed this message. (Canada 2002, 146)

One might well question the committee's conclusion that there is something wrong with Chapter 11 based on the volume of public criticism, but the voices of opposition have been heard in the country and certainly in the corridors of Parliament. Many civil society groups and special interests have expressed doubts over Chapter

11 and have done so in the face of what is a rather arcane area of public policy. These voices appear to have been strong initially in Canada and Mexico, but are also evident and growing now in the United States.

If the debate, however, has become a wide public one, how informed is it? So many arguments have been raised over investor protection in the last few years that there is a sense that the debate involves more than just investor protection. As Howard Mann, a severe critic of Chapter 11 says: "For some, Chapter 11 is a vital requirement in promoting the free flow of capital in an increasingly open North American market. For others, Chapter 11 represents another kind of bankruptcy of public policy and international law-making in the era of economic globalization" (*Private Rights* 2001, 1). Many critics raise issues: in this volume Stephen Clarkson focuses on the impact or threatened impact of globalization on national decision-making and national sovereignty. I shall come back to that wider debate. But first let us take a quick look at some of the data on the investor protection cases.

The summary data that follow (current as of the end of October 2005) suggest that the fears and criticisms appear to have been far greater than the actual consequences of the Chapter 11 cases. These tables cast considerable doubt on the civil society concerns. Table 1, for example, identifies the total cases. Over the 11 years and against all three governments, a total of 41 Chapter 11 complaints have been raised. These numbers fail to represent anything approaching a flood of cases. However, even this data summary exaggerates the number of actions against the NAFTA governments. A closer look shows that only 23 have actually reached arbitration stage. And when we identify only the actual decisions, the data reveal that just 15 cases have reached an arbitral decision including two that were settled prior to judgement.

Most telling, however, is the fact that of those cases where a decision has been reached (Ethyl Corp. actually settled before a decision by the tribunal was rendered) only six have resulted in the investor successfully obtaining damages. Moreover, the amounts awarded are limited. Barry Appleton in his chapter writes that the tribunals have awarded some US$29 million in

Table 1: *Complaints and Decisions under NAFTA Chapter 11*[1]

Complaints versus Canada

Name of Investor	Nationality	Status[3]
Signa S.A. de C.V.	Mexican	Not reached arbitration yet
Ethyl Corp.	American	Settled before arbitration's conclusion
S.D. Myers, Inc.	American	Successful claimant award
Sun Belt Water, Inc.	American	Not reached arbitration yet
Pope & Talbot, Inc.	American	Successful claimant award
United Parcel Service of America, Inc.	American	Reached arbitration
Ketcham Investments, Inc.	American	Not reached arbitration yet
Trammel Crow Co.	American	Settled before arbitration's conclusion
Crompton Corp.	American	Not reached arbitration yet
Peter Nikola Pesic	American	Not reached arbitration yet

Complaints versus Mexico

Name of Investor	Nationality	Status
Halchette Distribution	American	Not reached arbitration yet
Metalclad Corp.	American	Successful claimant award
Robert Azinian et al.	American	Dismissal of claimant
Marvin Roy Feldman Karpa	American	Successful claimant award
Waste Management, Inc. 1	American	Dismissal of claimant
Waste Management, Inc. 2	American	Dismissal of claimant
Adams et al.	American	Not reached arbitration yet
Lomas Santa Fe Investments, L.P.	American	Not reached arbitration yet
Fireman's Fund Insurance Co.	American	Dismissal of claimant
Calmark Commercial Development, Inc.	Canadian	Not reached arbitration yet
Robert J. Frank	American	Not reached arbitration yet
GAMI Investments, Inc.	American	Dismissal of claimant
International Thunderbird Gaming Corp.	Canadian	Reached arbitration
Corn Products International, Inc.	American	Reached arbitration (consolidation rejected)
ADM, Inc.	American	Not reached arbitration yet (consolidation rejected)
Francis Kenneth Haas.	American	Not reached arbitration yet
Texas Water Claims	American	Not reached arbitration yet

Table 1 continues on next page

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[1] I am grateful to Sergio Puig de la Parra for his willingness to allow me to use some of his data on Chapter 11 that he has gathered for his PhD thesis at Stanford University, tentatively named, "The Impact of NAFTA Chapter 11 Dispute Resolution Mechanism at Ten: Legitimacy, Evaluation and a Claim for Transparency." I have added some data and focus and I have altered the analysis in a number of cases for which he is in no way responsible. However, Sergio undertook the initial data gathering that was then adapted for tables 1 through 4. The cases identified are current cases of October 2005.

Table 1: *Complaints and Decisions under NAFTA Chapter 11 cont'd.*

Complaints versus U.S.

Name of Investor	Nationality	Status
Loewen Group, Inc.	Canadian	Dismissal of claimant
Methanex Corp.	Canadian	Dismissal of claimant
Mondev International, Ltd.	Canadian	Dismissal of claimant
ADF Group, Inc.	Canadian	Dismissal of claimant
Canfor Corp.*	Canadian	Reached arbitration
Kenex, Ltd.*	Canadian	Not reached arbitration yet
Doman Industries, Ltd.	Canadian	Not reached arbitration yet
Tembec Corp.*	Canadian	Reached arbitration
Glamis Gold, LTD.	Canadian	Reached arbitration
James Russell Baird	Canadian	Not reached arbitration yet
Grand River Enterprise Six Nations Ltd	Canadian	Reached arbitration
Canadian Cattlemen for Fair Trade	Canadian	Not reached arbitration yet
Hemp Oil Canada Inc.	Canadian	Not reached arbitration yet
Terminal Forest Products Ltd.*	Canadian	Reached arbitration

Note: * The three cases — Terminal Forest Products Ltd., Canfor Corporation, and Tembec Inc. were consolidated by an order of the Consolidation Tribunal pursuant to Article 1126 of NAFTA on September 7, 2005.

damages. Unless one suggests that any damages awarded pursuant to Chapter 11 are too much, and I suspect that there are critics who would be willing to do so, the total amount of damages awarded has been modest. Moreover, what is very apparent is that the concerns and the fears expressed appear to be out of proportion to the awards successfully obtained by claimants.

In looking at the cases and the criticisms raised, there appears to be a pattern of attack against Chapter 11. Various interests and other civil society groups appear to focus on complaints where there has been little progress in the case. In other words, criticisms have been built on speculation over the possible results in the cases. Critics have been quick to suggest the worst possible results, without assessing the likelihood of the outcome.[2] A number of cases have raised serious fears in civil society over such matters as the possible impact on the environment. One such case is *Methanex*. This case against the United States concerns the banning of a gasoline additive by the State of California. Yet the case went through an extended jurisdictional phase and the final award rendered on August 9, 2005 dissmissed the case with costs to the United States Government. Another case that has raised significant fears has been the *Sun Belt* case. This case against Canada concerns the export of bulk water from British Columbia to the United States — a hot-button issue if ever there was one. Yet by 2005 the case has failed to progress to arbitration.[3]

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[2] In the Public Citizen Chapter 11 report (Public Citizen 2005, vii), it declares that US$35 million have been awarded by NAFTA tribunals or governments as part of a settlement to foreign investors, and that US$28 billion has been claimed by NAFTA investors. The latter amount is simply a compilation of the data of damage relief sought.

Since the tribunals have only the power to award damages, although this is not always made clear by critics, cases are often cited for the damages demanded by claimants. The *Methanex* case, now dismissed, has often been cited as well for the excessive claim — in this instance US$1 billion. In general, the monetary claims in the pleadings have been the basis accepted by critics, notwithstanding the fact that the cases suggest that in the few instances where tribunals have awarded damages, the awards have been a fraction of the damages sought.

Accompanying this worst-case mentality, critics charge that Chapter 11 has caused a regulatory chill, especially with respect to environmental regulation. Stephen Clarkson argues strongly that Chapter 11 cases have discouraged governmental policymaking. As he writes in his chapter, governments are warned away "from taking policy and regulatory initiatives that respond to democratic demands even if they are entirely legitimate under Canadian law." Stephen Brereton in his chapter was drawn to rebut such generalized charges. This included a claim that Canada had passed only two environmental regulations through the period. He noted instead that over 40 environmental measures had been put in place by federal authorities by the end of 2004.

The regulatory chill charge is in the end difficult to assess. In determining regulatory chill the analyst is forced partly to prove the negative. One example is the rather infamous cigarette packaging case. Stephen Clarkson makes reference to it. According to

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[3] The Notice of Arbitration was filed on October 12, 1999 and it appears that no further steps were ever taken in the matter.

Clarkson: "An illustrative case is Ottawa's debacle over cigarette packaging." The critics argue that the federal government considered prohibiting brands, instead of requiring generic packaging for all cigarettes. But, as Clarkson points out, no case was ever raised against the federal authority. He draws the conclusion that the effort was abandoned as a result of manufacturers' threats to undertake a Chapter 11 case. While it is possible that the federal government was deterred by threats of action pursuant to Chapter 11, there are equally plausible alternatives, as well. Not the least of these is that government action could be undertaken without recourse to eliminating cigarette packaging. Still, these alternative explanations have failed to dent the views of those who believe Chapter 11 imposes a regulatory chill.

Environmentalists have been among the most persistent critics of investor protection in North America. Indeed, a number of claims had environmental aspects to them. But as Table 2 reveals, there are a wide variety of measures that have been targeted in the Chapter 11 cases, including tax policy, trade, customs, and procurement policy. Moreover it is often difficult to characterize the nature of the claim. For example, Barry Appleton in his chapter points out that the highly contentious *Methanex* case may have an environmental measure at the core of the claim, but it is also about "a failure to observe due process considerations by the State of California." While recognizing the multiple aspects of many of the cases, it still does not appear that environmental measures are the principal target of investor actions.

Table 3 turns to various government targets. Critics and officials of the sub-national governments of the NAFTA countries have expressed concern that Chapter 11 imposes obligations and restraints on them that they were never asked to assume. Municipalities, in particular, have expressed concern following the *Metalclad* (Final Award, April 25, 2000) case that investors using Chapter 11 will unreasonably impede municipal authorities in implementing measures in the public interest. Yet in only three cases have complainants sought damages from municipal authorities for possible breaches of the NAFTA obligations. And overall, in only eight cases have complainants brought actions against any government

Table 2: *The Sectoral and Policy Focus of Claims under NAFTA Chapter11**

Name of Investor (Canada)	Sector of Investment	Interest in Dispute
Ethyl Corporation	Energy: fuel additive	Environmental policy, trade policy
S.D. Myers, Inc	Services: toxic disposal	Environmental policy
Pope & Talbot, Inc.	Production: forest products	Administrative regulation
United Parcel Service of America, Inc.	Services: parcel delivery	Competition
Trammel Crow Co.	real estate management procurement policy	
Name of Investor (U.S.)	**Sector of Investment**	**Interest in Dispute**
Loewen Group, Inc.	Services: funeral	Judicial fairness
Methanex Corp.	Energy: fuel additive	Environmental policy
Mondev International, Ltd.	Services: real estate	Regulation and public liability
ADF Group, Inc.	Commercial: steel fabrication	Procurement
Canfor Corp.	Production: forest products	Contingent protection: trade policy
Terminal Forest Products Ltd.	Production: forest products	Contingent protection: trade policy
Tembec Corp.	Production: forest products	Contingent protection: trade policy
Grand River Enterprise	Commercial: Cigarette	Competition and regulation of tobacco
Glamis Gold, Ltd.	Production: minerals	Environmental administrative policy

Table 2 continues on next page

below the national or federal level. In addition, Table 3 reveals that the vast majority of cases are targeted at the executive branches of the various NAFTA parties.

Table 4 turns to a summary of the cases and the claims brought by investors against the NAFTA governments. Given the objective of NAFTA Chapter 11, it is not surprising that expropriation has been raised more frequently. What became more contentious, however, with respect to Article 1110 was the use of "tantamount to expropriation" in the provision. Stephen Clarkson, drawing on Schneiderman (1996), argues that this phrase "was itself tanta-

Table 2: *The Sectoral and Policy Focus of Claims under NAFTA Chapter11* cont'd*

Name of Investor (Mexico)	Sector of Investment	Interest in Dispute
Metalclad Corp.	Services: waste-disposal	Environmental policy
Robert Azinian et al.	Services: waste-disposal	Environmental policy
Marvin Roy Feldman Karpa	Commercial: cigarette exportation	Tax policy
Waste Management, Inc. 1	Services: waste-disposal	Environmental policy
Waste Management, Inc. 2	Services: waste-Disposal	Environmental policy
Fireman's Fund Insurance Co.	Services: insurance	Insurance regulation
GAMI Investments, Inc.	Commercial: sweeteners industry	Agro-commercial policy
International Thunderbird Gaming	Services: wager games	Regulation of gaming
Corn Products International, Inc.	Production: sweeteners industry	Tax policy
Robert J. Frank	Commercial: land developer	Property regulation

Note: * The cases cited here are only those that have settled or reached arbitration.

mount to a new constitutional property right, but one that was only available to NAFTA party subsidiaries of foreign-based [trans-national corporations]." Milos Barutciski in his chapter notes that ambiguity surrounds this right and that the "tantamount" phrase leaves unclear where the line is between expropriation and the government's power to regulate without potential liability for expropriation. He suggests that this phrase raises the prospect, again, of a chilling of government action, thereby possibly inhibiting the exercise of power in the public interest. But as he also observes, despite the fears raised by this phrasing in Article 1110, tribunals have rejected almost all claims for expropriation. Also he notes "that much of the hand-wringing about this issue to date is not warranted by the jurisprudence, which is on the whole quite conservative." Yet Canadian politicians, including former Foreign Affairs Minister Bill Graham, a well known international lawyer, have raised a concern that the expropriation clause is potentially too broad.

Table 3: *Government Respondents**

Name of Investor	Branch	Level
Metalclad Corp.	E	N, P & M
Robert Azinian et al.	E & J	N & P
Marvin Roy Feldman Karpa	E	N
Waste Management, Inc. 1	E	N, P & M
Waste Management, Inc. 2	E	N & M
Fireman's Fund Insurance Co.	E	N
GAMI Investments, Inc.	E	N
International Thunderbird Gaming	E	N
Corn Products International, Inc.	L	N
Robert J. Frank	E	N
Loewen Group, Inc.	J	P
Methanex Corp.	E & L	P
Mondev International, Ltd.	E & L	P
ADF Group, Inc.	E	N
Canfor Corp.	E	N
Grand River Enterprise	E	P
Terminal Forest Products, Ltd.	E	N
Tembec Corp.	E	N
Glamis Gold, Ltd.	E	N & P
Ethyl Corp.	L	N
S.D. Myers, Inc.	E	N
Pope & Talbot, Inc.	E	N
United Parcel Service of America, Inc.	E	N
Trammel Crow Co.	E	N

Note: 'E' stands for Executive, 'L' stands for Legislature, and 'J' stands for Judiciary. Level refers to the level of government. 'N' stands for national or federal; 'P' stands for provincial or state; and 'M' stands for municipal.

* The cases cited here are only those that have settled or reached arbitration.

Perhaps somewhat more surprising are the large number of claims raised over the matter of the minimum standard of treatments. Article 1105 is designed to provide standards of treatment for investors in accordance with international standard. For the NAFTA parties the use of this standard has proven galling. It rep-

Table 4: *The Substantive Claims**

Article	Description	% of Claims identifying breach of substantive obligation**
1110 Expropriation and Compensation	No Party may directly or indirectly nationalize or expropriate an investment of an investor of another party in its territory or take a measure tantamount to nationalization or expropriation of such an investment (…), except: (a) for a public purpose; (b) on a nondiscriminatory basis; (c) in accordance with due process of law and Article 1105(1); (d) on payment of compensation...	91%
1105 Minimum Standard of Treatment	Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.	85%
1102 National Treatment	Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors…	72%
1106 Performance Requirements	No Party may impose or enforce… requirements, or enforce any commitment or undertaking, in connection with the establishment, acquisition, expansion, management, conduct or operation of an investment of an investor of a Party or of a non Party in its territory.	23%
1103 Most-Favorable Treatment	Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to investors of any other Party or of a non-Party…	22%
Others	1104 Standard of treatment 1405 National treatment in connection with financial services 1502 Monopolies and state enterprises 1503 State enterprises	4%

Note: * The cases included here are only those that have settled or reached arbitration

** Investor claims frequently ground action against State with multiple substantial breaches.

resents an obvious international standard embedded in the overall investor protection provisions. It noticeably irritates the U.S. and the Canadian governments. There appears to be a longstanding view from officials of both countries that the Chapter 11 investor protections were designed primarily to assist investors in Mexico. From this perspective it was more than surprising that investors raised claims against these two developed countries, including the breach of the international standard of treatment obligation. A notable example of this irritation is seen by the U.S. reaction to the Loewen (Final Award, June 26, 2003) case that raised questions about the fairness of the judicial process in the State of Mississippi.

As Table 4 shows, the national treatment provision is the next most frequently used basis of claimed breach of Chapter 11 NAFTA. This section is a traditionally trade-based protection now extended to investment. The other bases of possible Chapter 11 claims drop off significantly in frequency. These substantive protections represent a limited challenge to the measures enacted by the NAFTA governments.

It is hard to summarize the many micro aspects that critics have raised over the Chapter 11 provisions. Legal experts, many civil society groups, and, increasingly, politicians in the three countries have publicized legal and political and policy objections and fears over the Chapter 11 investor protection provisions.[4] Most recently these criticisms have been expressed in the context of the ten-year reviews of NAFTA. Experts, but especially politicians in all three NAFTA countries, have voiced negative views, particularly with respect to jobs and prosperity, arising presumably from the consequences of NAFTA's implementation in their individual countries. As for specifically Chapter 11, the criticisms, though strong, have somewhat abated. And as noted, an examination of the evidence does little to support the fears expressed over the decade by critics. NAFTA Chapter 11 does challenge government action and subject it to wider standards. But as Milos Barutciski points out:

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[4] The criticism is certainly not dead. Recently in Canada, the Canadian Union of Postal Workers and the Council of Canadians launched a constitutional challenge to NAFTA's Chapter 11 in Ontario's Superior Court of Justice.

> A review of the limited jurisprudence to date suggests many of the fears unfounded that corporations could use Chapter 11 to bludgeon governments into paying massive compensation for implementing programs and legislation in the public interest. ...It is particularly notable that the Chapter 11 right that has been used to the greatest effect to date is the minimum standard of treatment under Article 1105, which has been successfully invoked on several occasions to remedy government conduct that was clearly arbitrary or capricious. That such conduct is constrained by Chapter 11 is most assuredly a positive development.

Fears of the sort expressed over Chapter 11 NAFTA should not be dismissed out of hand. Still, the critique on investor protection does appear to be highly speculative and work exaggerated in the face of the actual course of investment protection cases. Many of the concerns expressed by civil society groups, or their counsel, as well as legal experts, have failed to materialize. The process and substantive protections have been treated generally with a restrained touch by tribunals. Most claimants' successful actions have been grounded on identifiable capricious and arbitrary behaviour by government officials. The chilling effect on governments continues to be asserted; however, government officials reject such charges. At worst, government officials from the three NAFTA parties find it necessary to examine their actions against investor protection claims and, presumably, satisfy themselves that their policy meets the obligations set out in NAFTA. Such an obligation certainly does not appear to be an overwhelming one, especially for a government such as Canada's, where the development of a rules-based system is at least rhetorically strongly supported.

Where Is the Policy in Canada's Trade and Investment Policy?

In the rising criticism and debate over Chapter 11 NAFTA protections, an apparent turning point was reached with the agreement of the three NAFTA parties to interpret Chapter 11 protections pursuant to Article 1131. On July 31, 2001, the commission published its first Interpretive Note (NAFTA 2001). In that announcement the trade ministers of the three NAFTA countries exercised their right to "interpret," as they saw it, the provisions in Chapter 11. The commission sought to clarify the meaning of the minimum standard of treatment, Article 1105, and to clarify the transparency provisions under Chapter 11. This Interpretive Note came at the end of a series of critical statements over Chapter 11 protections by trade officials, including then-Minister of International Trade Pierre Pettigrew. This action by the trade ministers undermines Canada's long-standing invocation of the first principle of Canada's trade and investment policy — support for a rules-based global trading system and as a central feature of that rules-based global trading system, support for the rule of law.

The Ambivalent Defence of the Rule of Law

Canadian politicians and officials are constantly reminding the public and other nations in the global trading system of Canada's open economy. Stephen Brereton, in his chapter, reviews a variety of figures that reveal Canada is far more dependent on trade than other developed economies such as the United States and even Japan. To underline this evident economic reality, the former Minister of International Trade Pierre Pettigrew, in a moment of hyperbole possibly, in one of his last speeches ministering the portfolio, said of Canada's reliance on trade: "But Canada is a country of trade. I mean we are the trading nation on the planet" (Pettigrew 2003).

Notwithstanding the exaggeration, it is evident that Canada is, and has been, deeply enmeshed in the global trading system over the decades since the end of World War II. While Canada's trade may be highly skewed in the direction of the United States, the country remains deeply involved as an international trader with an economy highly dependent on export trade. According to Brereton, Canada has sought a level of openness in investment regimes to reflect Canadian interest in direct foreign investment, whether from inflows or Canadian investment abroad. As the minister stated in his speech to our conference:

> There is no doubt today that foreign direct investment in Canada ... and Canadian investment abroad have joined the international trade in goods and services to become our vital engine of growth and job creation.

And as a major trading country, but one with something less than major power status, Canada has been a consistent supporter of rules-based (including investment) systems of international governance. Brereton adds that for Canada, as opposed to, say, the United States, our most important trade and investment partner, a rules-based system for investment is the way to "provide a framework of disciplines, and encourage efficient resolution of disputes and greater consistency in legal and policy regimes. These rules also offer a greater measure of security for Canadian investors through assurances that national policies will not be changed unduly or applied in a discriminatory manner." Then the director of investment trade policy concludes:

> Canada has long been a supporter of a rules-based trade and investment system (where agreed rules regulate the flow of goods, services and investment) rather than a power-based one (where economic or military might dictate results), with the objective of bringing the investment regimes in other countries to Canada's level of openness.

Over the decades Canada has pressed for the development and elaboration of a rules-based global trading system. Our politicians and our government officials are well aware that, as a middle power and in the face of the dramatically greater economic and military power of our southern neighbour, Canada is more advantaged by far when a rules-based system dominates, whether in trade or in investment.

Michael Hart, a former Canadian trade negotiator, has summarized Canada's promotion of rules-based global regimes:

> Over the past six decades, Canada has been a pre-eminent leader in promoting, negotiating, and accepting a rules and regime-based system for the conduct of international relations. The drivers of Canadian rule-making and institution-building are Canada's perception of itself as a country whose most intimate foreign relations are with powerful countries that, unrestrained, will take little account of, or even damage, Canadian interests. Hence, the instinct to resolve problems through international rules and regimes has been a constant factor throughout the whole range of Canadian foreign policy endeavours. (Hart 2003, 12)

Yet the Liberal government's attitude toward Chapter 11, what I have called elsewhere Canada's *but-approach* to investment protection under Chapter 11 (Alexandroff 2004, 463–474), and the action by the NAFTA governments to exercise their so-called interpretive powers, leaves one gasping at what appears to be the undermining of the rule of law by the Government of Canada. This apparent action against interest is further demonstrated by the Canadian government's seeming eagerness to request judicial reviews of the cases decided against it and to support efforts by other NAFTA governments seeking judicial reviews where tribunal decisions have resulted in judgments against them.

The Canadian federal government has been ambivalent about the investment protection provisions as they apply to it. The chapters by officials in this volume reflect this but-approach. The former minister and his officials were sensitive apparently to the need to protect private investment interests. They insisted that investors need to be protected from arbitrary or discriminatory actions by governments in the NAFTA and beyond. As the minister said at the conference, "This is key to increasing our productivity and our prosperity." On the other hand the minister and his officials were determined to be able to set policy "in the public interest on environmental, cultural, and social issues," and that such powers not be compromised. Such a balance appeared upset as soon as a number of decisions were concluded that led to damages being awarded against the government. As the then-trade minister Pierre Pettigrew wrote in the National Post:

> We believe that several recent NAFTA tribunals have made errors when dealing with certain Chapter 11 cases, often overstepping their authority and taking unusually broad interpretations. In our view, they have read into the chapter ideas that the NAFTA drafters simply never intended. Some suggest that these misrepresentations, if not corrected, could be used to thwart important public policy objectives. For these reasons, the Government of Canada has taken actions to ensure that decisions of NAFTA tribunals interpret Chapter 11 as its drafters intended. (Pettigrew 2001b)

But how then is the balance to be identified? The mechanism became obvious soon afterwards — motions for judicial review and then the commission's Interpretive Note. Assuming that the original intent of the drafters is not readily knowable, notwithstanding the commission's assertions, where is the appropriate line between private and public, and how is it to be assured by the NAFTA governments? The line was hazily drawn in that same newspaper column, with the minister concluding his analysis by saying:

> It is very important that investors be protected from arbitrary and unfair actions by governments, but when investors' interests run contrary to the public interest, public policy — as long as it is openly arrived at and fairly applied — should prevail. (Pettigrew 2001b)

What the minister appeared to be suggesting was that as long as the measure — read that as law, regulation, or policy — was arrived at openly and made transparent, investor claims should not be able to prevail against a NAFTA government. Public purpose, in other words, would trump private interests: a wide ambit indeed that would eliminate all but the most egregious of cases.

As Laird argues in his chapter, the governments appeared intent on righting this balance by way of commission interpretations through Article 1131 and through judicial review motions, a number of which have been taken to Canadian courts as noted earlier. As Laird says, the commission's action was designed to "deflect criticism of NAFTA Chapter 11, and to narrow the playing field for Chapter 11 claimants, current and future, by limiting the substantive legal liability of the NAFTA parties." The NAFTA governments have argued publicly and before the tribunals that the clarifications are binding not just in the future but immediately and to cases under consideration by tribunals. Thus, the clarification and possibly future ones can be directed to alter conclusions where the governments are the respondents to investor claims. It is apparent that the Government of Canada believes that Article 1131 remains an instrument open to governments, in Laird's words, to "ensure that the provisions of the agreement are well understood." Such action by government cannot but undermine the rule of law. Though tribunals have given some indication that they may not be cowed into accepting such commission statements, the actions by the governments do potentially interfere with decisions in which they are a party.

The aggressive use of judicial review by the governments in the face of contrary decisions also is a trend of some concern to those determined to protect investment in the three NAFTA countries. In the case of Canada, the government made submissions on the *Metalclad* review and brought action against the *S.D. Myers* (Partial Award, November 13, 2000) decision. Some have argued of course that it is unreasonable to presume that governments will not act in the face of a right granted through Chapter 11. But the concerns have arisen in part because the reviews appeared more as full appeals. Also, concerns were raised when Ottawa argued in its submissions that these international tribunals should be accorded a minimum of deference. These concerns were only reinforced when a single judge of the British Columbia court, the Honourable

Justice Tysoe, appeared to render a decision that interpreted international law, notwithstanding his injunction against doing so.

The concern of international arbitrators has been somewhat mollified in two Federal Court judicial reviews that dismissed both a judicial review brought by Canada in the *S.D. Myers* case and a Mexican judicial review brought in the *Feldman* case. Nevertheless, the actions by the NAFTA parties, Canada in particular, have raised questions over its commitment to the rule of law in investment protection. The ambivalence of the three governments is captured well by Milos Barutciski in his chapter. He describes the ambivalence as: "the three NAFTA governments — Canada the United States, and Mexico — sit strangely noncommittal on the sidelines and more than a little defensive, making reassuring noises about the importance of investor protection, punctuated by periodic hand-wringing over 'rogue panels' and the need for greater 'clarity' to reinforce their 'true intent' in negotiating Chapter 11."

The NAFTA parties may indeed believe that there are required clarifications to Chapter 11. If so, the commission should take the necessary steps to set out what it believes to be the appropriate interpretation. And then the commission should forsake additional clarifications to lift the cloud of ever-present action against tribunal decisionmaking by the NAFTA parties. The rule of law would be much better served through such finality.

The "Strange Death of Liberalization" in Canada's Trade and Investment Policy

With apologies to historian George Dangerfield,[5] this section tries to understand the ambivalent attitude that has crept into Canada's policy on investment protection but, as suggested here, even more broadly on Canada's trade and investment policy. For decades, Canadian policy has favoured trade liberalization and the elimination of barriers that impede the relatively free flow of goods, services, and capital. This is not to suggest that Canada, like other countries, did not do its level best to protect select producer interests whether agricultural, cultural, or other. But overall, the major trading countries, including Canada, could be counted on to make necessary and sufficient sacrifices to advance trade and investment liberalization. Yet the but-approach to investment protection and the emergence of a process and consultation-oriented trade and investment policy signalled an apparent cooling by the Government of Canada towards free trade.

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[5] George Dangerfield wrote a well-known study of the demise of the Liberal Party in Great Britain at the end of the nineteenth and the beginning of the twentieth centuries (Dangerfield 1961).

Pierre Pettigrew's tenure as Minister of International Trade bookends the critical multilateral negotiations — the Seattle ministerial meeting in 1999 to the Cancun session in 2003. Both the beginning and the end of his tenure were eventful, as were many of the trade and investment issues that faced the minister and his officials through the turn of the twenty-first century. It is evident from the minister's speeches, however, that the emergence of antiglobalization protests, first at Seattle and then at meetings afterward, shocked him and caused him to reflect on the societal and political forces, as well as trade interests, facing him and his officials. Probably no incident, however, was more striking than the Seattle meeting, which became known as the 'Battle for Seattle.'

Describing Seattle in his Manion Conference speech in 2000, the minister described the Battle for Seattle this way:

> What happened in Seattle? What I saw in Seattle is two worlds that met — one might almost say collided. Two international orders finally met: the traditional one, the international world of the states that were getting together to negotiate among themselves the launch of a new trade round and the globalized world. (Pettigrew 2000b)

The minister was aware of the contending approaches between government efforts to extend free trade or more precisely the liberalization of trade and investment and the non-governmental organizations (NGO) and civil society groups vocally, and sometimes physically, opposed to the negotiation of free trade.

> Who can deny that the intention at Seattle was to remind us of the human purpose of economic activity? Who can deny that the political leaders there were sent back to do their homework, with instructions to be true to the humanistic values that the West so strives to promote? … In short, who can deny that a new model came to light in Seattle? (Pettigrew 2000b)

It is the description of that new model by the then-minister that leaves one slightly at a loss as to how a government trade policy was likely to be fashioned from such a difficult and amorphous concept, as described below:

> The change we are witnessing could perhaps best be described as a shift from an ethic of justice — cold and technocratic — to an ethic of care. … I believe that the challenge is less about changing the world and a lot more about being compelled, by the forces of globalization, to change or reshape our lives to adapt to the new era. (Pettigrew 2000b)

Though Pettigrew was searching apparently for a new trade and investment policy that might somehow address the antiglobalization interests and groups, he appeared in the end to abandon the principal motivation underlying Canadian trade and investment-policy trade liberalization:

> With regard to the new altruistic values that we have to establish, we must however be realistic and acknowledge that the spirit of free trade will not be much help to us. For objective concurrence between commercial openness to others and the financial advantages of the openness does not exist where the issue is the establishment of new values and the common good, as it did exist when free trade was being established. (Pettigrew 2000b)

The Manion Conference speech was the most dramatic expression of the minister's effort to come to terms with the antiglobalization opposition to trade liberalization. But the minister spoke on a number of occasions subsequently of his changing view of trade and investment policy. In Britain the following year, he continued along a line of thinking that appeared to shift his views of trade from liberalization to social and political concepts as the foundation for trade and investment policy:

> We must demonstrate that once again when we want trade, our goal is not just to benefit the big corporations. It's political stability. It's democracy that we are after when we want to build a strong rules-based system. (Pettigrew 2001a)

These remarks at the Royal Institute for International Affairs were prepared also, it would seem, so that the minister could assess the progress of multilateral World Trade Organization (WTO) talks, as well as regional, primarily western hemispheric talks, on the Free Trade Area of the Americas (FTAA) post-Seattle and then Quebec City. According to the then-minister, broad progress had been achieved in the FTAA talks since Seattle in the area of trade liberalization, but in those areas that, as he put it, "complement freer trade." This progress was something that the multilateral discussions might well take note of in the effort to advance the new round of trade negotiations. Tellingly, Pettigrew then suggested that there were three lessons specifically that he could take from Quebec City:

- A commitment to transparency;
- Increased openness, inclusion, and dialogue; and
- Concerns of less-developed economies.

As is evident, Pettigrew's focus in these remarks was principally on process. In particular, the second lesson focuses on consultation and dialogue with civil society groups and interests. As the minister argued, "Another lesson we have learned is to listen to protesters and their concerns" (Pettigrew 2001a). Not only was the minister trying to grapple with and accommodate the antiglobalization goals that were first openly expressed in Seattle, he was designing a policy that would openly engage these interests.

Such consultation and dialogue with protesters was presaged in the minister's remarks before the Commons Standing Committee on Foreign Affairs and International Trade on April 5, 2000 (Pettigrew 2000a). In those remarks he outlined the various actions the government was pursuing to engage civil society groups especially in the FTAA process. His remarks, among other things, chronicled the interactions that he and his officials had with civil society groups and the efforts that he had made to convince his hemispheric colleagues to undertake similar consultation and dialogue. As he pointed out in his prepared comments to committee members, he had convinced 22 colleagues at the Toronto FTAA ministerial meeting in November 1999 to join him in meeting civil society groups at the People's Summit that was organized to coincide with this FTAA Ministerial meeting. He noted prior to that meeting that representatives from only five countries had ever met with such groups. From the minister's perspective, this civil society effort was the key to a successful initiative on the government-to-government level — "They can serve as a new model for governments…" as he put it (Pettigrew 2000a).

There is a long list of such encounters over the period described by the minister. He saw such efforts by his officials and himself as promoting "the kind of trade Canadians want, as well as to demystifying the trade negotiating process" (Pettigrew 2000a). One of the consultation initiatives mentioned by the minister was the Seattle consultation meetings. As Pettigrew correctly points out, this was a daily briefing where the official delegation and also NGOs were in attendance before officials. As the minister proudly noted, following the meeting, half the delegation went to the official meetings while the other half "would get up to take their positions outside the convention centre to protest the deliberations! This was a truly Canadian moment!" (Pettigrew 2000a).

While it may well be exactly what the minister suggests, it does not constitute a trade and investment policy. I was fortunate enough to attend many of those Canadian information sessions at Seattle. What was apparent was that while the interests and the civil society groups were in attendance, they were there, principally, to watch and scrutinize every action by the minister and his officials. These groups were insistent before the minister and his officials that no compromises were possible on investment or on the specific agricultural sector they represented, or on a host of other issues including, as they saw it, the environment, labour, social, and cultural issues. It was these kinds of consultation processes that led my friends and colleagues at Seattle to conclude that the best name for the then nascent multilateral round should have been the Protectionist Round.

Here then was the new open consultation process. The problem was that most, if not all, civil society groups were there not to advance the trade and investment agenda but to stop the negotiation, or defend against liberalization in their area or in their sectoral interest, if not more widely. The minister and his officials were engaging groups that were opposed largely to advancing the negotiation, or reducing barriers, or indeed liberalizing trade policy — what had been the heart of Canada's policy since the inception of the General Agreement on Tariffs and Trade (GATT). This consultation process, apparently now at the heart of Canada's trade and investment policy, largely rejected efforts to liberalize Canada's policy. In the crafting of Canada's post September 11 trade and investment policy, two long-time trade negotiators, Bill Dymond and Michael Hart, noted the minister's and his officials' focus on groups that had no interest in liberalizing trade:

> Part of the government's initial coolness to a Canada-U.S. border initiative is the result of a continued fascination with claims of freer trade's opponents. Protestors, nationalists, environmentalists, human rights activists and other 'civil society' groups have captured the government's attention out of all proportion to their weight in society and their capacity to make constructive contributions. The government has been reluctant to accept that many of these groups are animated by values and preferences that most Canadians do not share and that deny the fundamental tenets of Canadian trade and foreign policy. As a result, during the first two mandates [of the Liberal government], the government sent out confusing signals about the need to accommodate their claims and preferences. (Hart and Dymond 2001, 34)

The substitution of a consultation process for liberalization in Canada's trade and investment policy became even less of a compass as events challenged our U.S., our regional, and indeed our multilateral policy initiatives. There is potentially a wide divergence between our national interest and our national opinion when it comes to, for instance, closer U.S. economic ties, and increasingly on security and border issues. But there appears to be no consistent trade initiative. Thus, at one instance the minister comments on a U.S. trade goal in 2002, saying:

> Now many in the business community have been calling for a strategic or a grand bargain with the U.S. Others have called for a common market or a customs union. While there is always room for a healthy debate, and I encourage it, I do not think that there is currently an appetite for such a grand scheme. (Pettigrew 2002)

Having suggested a big trade initiative is not supported by Canadians, he then goes on to identify six goals which, while not creating a customs market or customs zone, certainly would initiate a comprehensive trade program.[6] And then in contrast to the earlier expressed coolness to a broad U.S. initiative, following the collapse of talks at the Cancun meeting, Minister Pettigrew, in one of his last speeches as trade minister, relates that he turned to Bob Zoellick, U.S. Trade Representative, and said, "Bob, …Am I glad we have that free-trade agreement with you. Let's deepen that relationship even further. Let's trade with the people who want to trade" (Pettigrew 2003). In these remarks he went on to say:

> But when you see the setback we are having in Cancun with the WTO round of negotiation, you do have to realize that even if Canada's cornerstone of our trade policy remains the WTO, it is imperative that, of course, we take very good care of our trading relationship with NAFTA and in particular, with the United States of America. (Pettigrew 2003)

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[6] The six-point program's elements: (1) increase Canada's share of the U.S. market; (2) increase two-way flows of investment; (3) advance the smart regulation agenda; (4) bring trade remedy practice more in line with growing integration; (5) eliminate the border as an impediment to trade investment and business development; and (6) enhance our representation in the United States.

Towards the end of this speech, the minister once again repeats and offers as Canada's trade objectives, the six-point program he'd articulated the year before.

The attack on investor protection provisions in NAFTA is part of larger debate and protest over greater international economic integration, and the growing influence of global markets and multinational corporations on the lives of citizens. The debate has been loud and persistent. But the government's response — a continuing ambivalence over the consequences for Canada of Chapter 11, a policy that not unreasonably can be interpreted as undermining the rule of law appears inadequate and even a policy against interest.

The challenges posed by antiglobalization demonstrators are real and should be appraised. But in the end, Ottawa is unlikely to square the circle between opposition to liberalization expressed by antiglobalization groups and the broad public's continuing commitment to free trade. For Canada, a middle-ranked, open, developed economy, to appear to question or even potentially rebuff a trade and investment policy that favours continued global liberalization of trade and investment seems unthinkable. Even the appearance of such a strategy could at one and the same time harm our influence in the global trading system and potentially limit Canada's prospects for expanding its economic opportunities and its national prosperity.

Globalization, the Global Trading System and Investment

As much as some, maybe many, politicians might not wish it, investment is now intimately linked to international economic policy and prosperity, as is traditional trade policy.

John Hancock in his conference presentation described what for him at his perch at the WTO is an everyday experience:

> Investment is at the epicentre of global economic relations. It touches on — and crosses over into — issues related to trade, capital flows, macroeconomic policy, technology transfers,

> domestic regulation, and the complex interface between private and public interests. Increasingly, it is impossible to talk about the management of globalization without talking about global rules to help manage investment and capital flows. Nothing is more 'globalized.' Yet the defining characteristic of today's international investment architecture is its "un-global" nature.

In the multilateral setting, however, it would appear, at least on the surface, that there is strong opposition especially from the developing and least-developed member states to the extension of the covered agreements at the WTO to include investment protection in some form. Opposition to the so-called Singapore issues, including investment, has been significant.[7] Indeed it would appear that investment policy was a major stumbling block at the WTO ministerial meeting at Doha in 2001 and certainly at Cancun in 2003. At Doha, India took the lead in efforts to preclude investment from the Development Round. Strong opposition continued at Cancun. As a result, as described by John Hancock in his Prologue, a multilateral investment agreement cannot be negotiated as part of the Doha Development Round.

Certainly globalization or more precisely antiglobalization perspectives lie at the heart of opposition to investment protection and more broadly against traditional free trade agreements. Stephen Clarkson chronicles some of the many arguments against both investment protection and free trade. At the heart of his and other opponents' arguments lies opposition to international limitations on national decisionmaking that such agreements bring, as well as to the protection of foreign corporate investors. In describing Chapter 11 as an extra-constitution, Clarkson concludes, "The impact is to constrain the authority of Canadian governments at all levels as definitively, but more arbitrarily, than do the norms and limitations imposed by Canada's constitution and its common law."

The antiglobalizers emphasize the power of market forces and transnational corporations to constrain governments to the detriment of local governmental policy, broad social, as well as the political and cultural forces in the many member states of the global trading system. It is arguable, and taken up by both Lou Pauly and John Hancock in their chapters, whether it is market forces and economic integration that inevitably drive multilateral investment protection. Though there is a view that deeper economic integration drives multilateral investment protection, Pauly argues that political realism and the conditions negotiated by governments will inevitably determine the nature of the multilateral bargain.

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[7] The Singapore issues include investment, competition policy, procurement, and trade facilitation.

Sex without Love — Extending Investment Protection One Way or the Other

The visible multilateral resistance to investment protection is evident and widely acknowledged. Many member countries expressed pleasure that the Singapore issues were blocked from inclusion in the Development Round at the Cancun meeting in 2003. But there exists another reality. In the 1990s, there was a wide expansion of bilateral investment treaties (BITs). The United Nations Conference on Trade and Development estimates that there are now well over 2000 BITs, some 1,800 having been negotiated in the last ten years. More recently, the United States in particular, but other developed countries as well, have negotiated and signed bilateral free trade agreements, principally with countries in Latin America and in Asia.

These agreements generally include investor-protection provisions. And in the regional agreements being negotiated, or completed, the 2004 Central America Free Trade Agreement (CAFTA) and the much larger FTAA,[8] investor protection is included or at least on the negotiating table. So, though many countries took apparent delight in the blocking of the Singapore issues, many of these same nations are busily signing investor-protection provisions on a bilateral and regional basis. While this may satisfy a number of audiences inside and outside these governments, such action appears to harm those most in need of strong investment protection regimes. It creates an institutional structure that is overly complicated, opaque, and likely to undermine stability by creating the continuing generation of competitive preferences that may well distort economic allocation. Such a global economic system is likely not to favour those countries that are today most opposed to multilateral investment and yet most in need of investment. John Hancock in his conference remarks summarizes the dilemma of this possible patchwork of investment protection:[9]

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[8] Following the disasterous 4th summit at Mar del Plata, Argentina, it would appear that a hemispheric free trade agreement among the 34 countries of the Americas is unlikely to be concluded any time soon.

> The bigger danger arises when regionalism becomes a substitute for multilateralism — or worse when it serves as an instrument for carving out preferential access to key global markets. In a world where investment is key, not just to capital flows, but to flows of production, technology, and trade, regional arrangements that are discriminatory — in terms of rights of establishment, licensing requirements, certification, regulations and standards, and the movement of people — can give rise to conflict and impact negatively on global economic stability.

A Final Salute to Investment Protection

Christopher Wilkie, Deputy Director of the International Investment and Services Policy Division of Industry Canada, reviewed the Chapter 11 NAFTA investor protection provisions (Wilkie 2002). He argued in his review that the evidence makes it impossible to conclude that the investor provisions "have contributed to increasing investment flows to and from Canada" (Wilkie 2002, 33). In the current global trading system, governments benefit from a generalized business belief that most governments in the international economy are unlikely to act in a way that would fundamentally harm direct foreign investment. There is a general consensus that investors are unlikely to see their business opportunity expropriated or to have governments act in such a desultory way as to interfere fundamentally with the foreign business enterprise in the target market.

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[9] In a recent report to former Director General Supachai Panitchpakdi, the panel took a rather dim view of the spreading regional agreements (Consultative Board 2005).

Though Wilkie may be right that it is not possible to show the relationship between investor country choice and the availability of strong investment provisions, it remains likely that poor treatment directed at foreign investors is a significant deterrent to continuing foreign direct investment flows.

For a country such as Canada, now a significant investor abroad and at the same time determined to be an attractive destination for direct foreign investment, behaviour that may colour country or regulatory risk would be, or should be, avoided by officials. Especially in the post-September 11th world, Canada has to be alert to any negative policies that might amplify the concerns already raised by heightened cross-border security steps. Such security concerns might already have weakened foreign investors' appetites to invest in Canada as opposed to the United States.

Thus, behaviour that might add to the uncertainty and increase investment risk to a foreign investor's decision seems an unhelpful approach by trade officials. It is disconcerting, then, to witness the ambivalence created around the but-approach to investor protection and principal Canadian values, especially protection and support for the rule of law. The trade ministers' continued use of Article 1131, especially for cases pending, is extraordinary. The right to interpret, or more likely, reinterpret what the substantive provisions of Chapter 11 originally meant is a right that North American governments generally, and Canada in particular, should forego. To encourage investors to continue to regard Canada favourably as an investment destination and to maintain and even improve the climate of treatment for Canada's investments abroad, politicians and Canadian officials must become unalloyed supporters of investment protection in North America and throughout the global trading system.

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INVESTOR PROTECTION IN THE NAFTA AND BEYOND:

Private Interest and Public Purpose

Alan S. Alexandroff, Editor

When the North American Free Trade Agreement (NAFTA) was signed, a provision was included to protect and encourage cross-border investments. It established that if the governments of Canada, Mexico and the United States fail to treat North American investors as they treat their own nationals, those investors could take their claims to international panels. The provision was relatively uncontroversial at the time of signing. Since then, however, observers have raised concerns that this provision restricts the right of governments to protect public policies in areas such as health, safety and the environment. This edited volume directly confronts the issue at the heart of this very heated debate: protecting the private rights of investors and attracting investment versus meeting public interests.

Leading academics and practitioners in the areas of investor protection and NAFTA examine the limited number of investor protection cases that have come before the international tribunals and place them within their larger context. In addition to pointing out some concerns, the commentaries ultimately reveal many positive aspects with respect to investor protection and the relative success of this provision in terms of public policy. Several contributions also explain and assess the tactics and strategy of the Canadian government. A few essays discuss the much-fought-over issue of investment and investment protection in multilateral negotiations, including the current Doha Round of the WTO.

The relevance of the investor protection mechanism in NAFTA extends far beyond North America and carries important lessons for the inclusion of such protections in bilateral, regional and multilateral free trade agreements. Another broader theme these essays raise: restraints on government policies and, ultimately, national autonomy in the face of continuing globalization.

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